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ANTONIN BASCH is well qualified to discuss Continental economy. His first contact with the economic problems of Central and Southeastern Europe was in the early Twenties, when he served as commercial attaché of the Czechoslovakian Legation in Berlin. He then taught economics in Prague for several years. In 1926 he became head of the Research and Central Banking Department of the National Bank of Czechoslovakia. He represented this bank in negotiating clearing agreements with Hungary, Austria, Yugoslavia, Germany, Rumania, and Bulgaria. He attended the World Economic Conference in Geneva and was Czechoslovakian delegate at the Bank of International Settlements at Basel. He was a member of the Economic Council of the Little Entente and of the Board of *Centre Economique*, established in Prague for the promotion of economic relations with the Danubian countries. From 1934 to 1939 he was managing director of the United Chemical and Metallurgical Works, which controlled leading chemical companies in Czechoslovakia, Hungary, Rumania, and Yugoslavia.

Dr. Basch came to the United States in 1940 and, after serving as visiting professor at Brown University, is now in the economics department at Columbia University. He was a member of the Czechoslovakian delegation at the Atlantic City, Philadelphia, and Bretton Woods conferences.

A PRICE FOR PEACE

HEALTHY markets for Europe's products are tied irrevocably to the peace, prosperity, and welfare of the post-war world. Pointing the way is this important, timely study of Europe's economy by a man who is thoroughly familiar with the problems involved. Dr. Basch first presents a clear analysis of the causes of the disruption of the Continental economy and shows how the dislocation of international trade will affect European nations and why full consideration should be given to the integration of Europe's economy, to the development of the backward countries, and to the interrelation of Germany and the rest of Europe, whatever the solution of the German problem may be. The author then explains how these unfavorable changes could be offset by an expanding trade with the Soviet Union, the Middle East, and other new markets; states the prerequisites for the maintenance and promotion of Europe's welfare; and points out the dangers threatening the peace if immediate action is not taken for concerted international assistance and expanding world trade as well as for an economic cooperation organized on a broad basis. As the world's strongest power the United States should take the initiative in such an action. This is a book for everyone concerned with the stabilization of Europe and a permanent peace. Foreword by James T. Shotwell.

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NEW YORK
MANUFACTURED IN THE U.S.A.

To MONIKA and JAN

FOREWORD

THE CENTRAL theme of this volume is stated in unmistakable terms at the opening of the second chapter: "Europe can maintain her standard of living, her level of production, and the welfare of her peoples only as an integral part of a well-functioning world economy." But the reverse of that statement is equally true and equally challenging: There cannot be a well-functioning world economy unless Europe is an integral part of it. Taken together, these two statements are a measure of the importance of the problems with which this volume deals. Moreover, the problems are as difficult as they are vast, for they have to do with the intimate affairs of the daily life of the common man under the varying conditions which have been determined by history as well as by the circumstances of the present and future. Thoughtful people, therefore, will appreciate and welcome such a survey as this, coming as it does from an economist who has had a unique opportunity to watch the development of European trade, industry, and finance in the years between the two World Wars, and who now views that scene in the perspective of world affairs. For Professor Basch has never suffered from the academic fallacy of regarding business as an abstraction for the theorist. The picture of Europe which is here presented is that of a real world, doubly tragic because of its reality and doubly important because of the pressing need for action to make the peace settlement a real and lasting one.

The devastation caused by the war is inevitably the first

matter of concern in any survey of present-day Europe. Even the disasters of the Thirty Years' War in Central Europe, which held back the development of Germany for over a century, have been far surpassed by those of the last five years, and we are by no means through the disasters and anarchy which may follow the war itself. Yet, as Dr. Basch points out, the processes of recovery are now so much greater than those in the pre-industrial age that the physical restoration of the homes and factories and cities of Europe may be surprisingly rapid. Science can destroy more quickly than it can rebuild, yet the rebuilding may also present miracles of achievement. But this reconstruction of Europe will not be real or lasting unless the economic life within it is sound and healthy; and it cannot be healthy in the era of scientific production unless the marketing of goods can escape from the fetters of economic nationalism. If, after the second World War, Europe and the world outside—for both are interdependent economically—repeat the tragic blunders of the 1920s and set up barriers to trade in an almost open economic warfare, then there is no hope for either prosperity or lasting peace.

While the blunders of the past offer little encouragement for optimism, it is also true that their lesson has not passed unnoticed among thoughtful people both in Europe and America. Whether the lesson of those blunders has been learned sufficiently, time alone will show. But it is at least clear to any student of the problem that the worst of all blunders would be postponement of the economic settlement. For, after the war is over, every day that passes will result in the creation of new vested interests along with the restoration of old ones, each of them narrowly fighting for its life without reference to or regard for the prosperity of others, without which its own cannot long endure. The time for the consideration of these issues is

now. For Americans it begins here, and not in Eastern Europe, for in the long run it is all one economy.

In the wealth of material which this volume offers, there is one subject which is of special interest, because it opens new perspectives. We tend to think of European economy in terms of the countries of Western Europe; but it is already evident that there will be a stirring of new life in the countries east and south of Germany. These countries are primarily agricultural. Now science is reaching out beyond industry to agriculture and will, without doubt, change the nature of rural life within the coming generation as definitely as it has changed that of hand industry in the course of the nineteenth century. Communications are also rapidly changing the geography of the whole world. The bearing of these facts upon the economy of Europe should not be lost sight of. For the backward areas of Eastern Europe which were left untouched by the commercial revolution of the sixteenth and seventeenth centuries will enter into a new era in the production and distribution of wealth. The resources of the far corners of the world will be made as readily available for these areas as was the case with Western Europe under the influence of ocean commerce. If these great reservoirs of economic possibility are successfully tapped by the new processes of invention, there will be less and less place in the world for the narrow provincialism of the past.

The economy of an interdependent world cannot succeed in the long run, however, without the assurance of continuing peace. The elimination of war as an instrument of national policy is therefore not an external but a fundamental part of the economy of nations.

JAMES T. SHOTWELL

New York
February, 1945

PREFACE

IT is certainly too early to try to evaluate the economic consequences of the present war in their entirety. It is not too soon, however, to collect the facts, to analyze them from various angles, and on this basis to prepare a firm line of international policy, so that the mistakes made after the last war shall not be repeated. This time we must make certain that economic problems receive the attention they demand.

The impact of the war will be heavier on the Continent of Europe than on other parts of the world; the task of reconstruction and rebuilding will be more difficult and complex. A common and general program of economic reconstruction and reorientation is, therefore, desperately urgent. The present study, which was sponsored by the Carnegie Endowment for International Peace, Division of History and Economics, attempts to outline and examine some of the more important problems of the European economy—the changes that Europe will face—particularly in its relations to the rest of the world.

In view of the many unknown factors in the political as well as in the social sphere, it could not be my aim to formulate a detailed program of reconstruction and adjustment. Nevertheless, an analysis of failures in the past and of changes in the world economy should serve as a guide for the major lines of policy. I shall be satisfied if this study serves to stimulate discussion that shall prove helpful in shaping the postwar economic policy in Europe.

I am very much indebted to Professor James T. Shotwell, who read the manuscript and gave me many valuable sug-

gestions. My sincere thanks go to Miss Matilda Berg of the Columbia University Press for her highly efficient help in editing the manuscript.

ANTONÍN BASCH

Columbia University
January, 1945

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CHAPTER ONE

PROBLEMS AND OBJECTIVES

IN PREPARING for a period of prolonged peace, the United Nations are concentrating a great part of their respective endeavors upon economic problems. Their leaders are well aware of the fact that without a satisfactory solution of crucial economic and social problems no lasting peace can be established. Those who are called upon to shape the basis of world economy after the war are going farther than did the peacemakers at Paris. One of their first objectives is to reach an agreement on some of the fundamental issues facing them. Moreover, they must organize the machinery vital to the rebuilding of world economy. A comprehensive program is, therefore, being discussed and devised to bring about security and freedom in the political as well as in the economic field.

We cannot yet fully evaluate or even grasp the economic and social consequences of the second World War. We can estimate approximately its direct financial and material costs. We know that the destruction of the economic machinery in continental Europe, in Great Britain, the Soviet Union, and in large parts of Asia will be great, and we know, too, that resources in human life and in economic productive capacity will be sadly depleted. But we also know that the world still possesses sufficient recuperative power to surmount these losses, and, even, within a rather brief period to surpass them with replacements. In fact, with economists and technicians of the caliber available in charge of the task, we could be fairly sure of success within the expected time. However, we cannot disregard the fact that other

than purely technical aspects will have their weight, perhaps sometimes fostering the program but very often presenting serious obstacles to it.

Certain common aims dominate any policy of postwar economy, aims that are everywhere accepted as desirable and as necessary to achieve. Hitherto, these have been expressed, for obvious reasons, in general terms. To implement them will be the task of national, and new international, bodies created for the purpose. Foremost among these objectives are:

1. An effective system of political security.
2. A policy of economic expansion that will ensure a high level of employment in the industrialized countries and promote economic growth in the retarded regions. This would presume an expanding world trade on a multilateral basis. An integral part of the program would be a rising standard of productivity and of living, and economic security to protect workers against such hazards as the mass unemployment of the thirties.

There can be no doubt that the great majority of European peoples will happily subscribe to these common economic objectives of the United Nations. But how will it be possible to carry them out in Europe? What will Europe's economic status be in the postwar world? It had already relatively declined after the last war and will be in a worse state after the present conflict ends. The problem of the economic rehabilitation of Europe is one of the most vital problems of the postwar world. Until it is settled there can be no equilibrium in the world economy.

When we speak here of Europe we have in mind continental Europe, excluding Great Britain and the Soviet Union. Though Great Britain and the economically most important part of the Soviet Union belong geographically to Europe, nevertheless their case differs from hers. It is true that Great Britain was the

greatest single purchaser of European exports, but it is also true that the larger part of her foreign trade was with other continents and that she received from other continents by far the greater part of her income from sources other than trade. Her investment in Europe amounted to only 8 per cent of her total foreign investments. As for the Soviet Union, her total foreign trade in the prewar period was no greater than that of Czechoslovakia, for example. Furthermore, because of her economic, social, and political structure and organization, she represents an independent unit forming a kind of continent by herself. Her problems have been and will be different from those of continental Europe.

Often the question is raised whether, even for the limited purposes of an economic analysis, it is appropriate to regard continental Europe as a unit. There are, for instance, Scandinavian economists who claim that their countries have little in common with the rest of Europe, that in economic background and in political and psychological outlook they are nearer to the United States and to Great Britain than to Southeastern Europe. Similarly, in the Low Countries there seems to be a tendency toward disentanglement from the destiny of the European Continent and toward alignment with some kind of community of the Atlantic countries. But though the nations of the Continent may entertain more or less intensive political, economic, and cultural relations with other continents, they cannot escape from the common fate of Europe. Even those countries in which the tendency toward disassociation is strongest have been greatly dependent on Europe in their foreign trade. This general interdependence was clearly demonstrated to the countries occupied by Germany, in spite of the fact that the Germans attempted to differentiate, in treatment, between Western and

Eastern Europe. Even the few neutral states have not escaped from the direct or indirect effects of the German domination.

What have been the particular features in the economy of Europe, and what will be the problems common to all its nations? To a greater extent than any other country except Great Britain, the countries of Europe have depended on trade with other continents for foodstuffs and raw materials needed to maintain the established standard of living. Without this multilateral international trade, employment in the industrialized countries cannot be maintained; without steady employment and prosperity in the advanced parts of Europe the agricultural areas are doomed to depression and poverty.

The peoples of Europe are politically more conscious than are peoples elsewhere. Now they are also aware that there are potentialities in the world economy to provide for a decent standard of living, for progress, and employment, everywhere. They are ready to demand the immediate organizations of a new and better-balanced world economy. And they are prepared to demand it with a very loud voice. Yet this continent, having suffered two cruel wars in one generation, will have to overcome greater difficulties to reorganize and rebuild its economic and social life than any other continent, Asia not excluded. These difficulties will be even greater than those expected in Great Britain, because the latter has not been occupied by the enemy and has preserved its political and social structure. And though Russia has suffered enormous human and material losses, she, too, will be in a relatively easier position than the ravaged Continent of Europe.

In speaking of rebuilding and reconstruction we do not refer only to the enormous immediate postwar task of relief and rehabilitation, and the repatriation of many millions of displaced

persons. Of course, the devastated areas will have to be rebuilt, the exhausted supplies of food and raw material will have to be restocked, and transportation reorganized; but over all these problems there is the foremost task of fitting the Continent of Europe into the new structure of world economy. The period between the two wars has not sufficed to adapt Europe to the economic changes throughout the world. This time the task of readjustment will be even more difficult. Trade with other continents must be adjusted, and, in view of the altered status of Europe's most important trading partners, there will also be important changes in intracontinental trade. The magnitude of this purely economic task must not be underrated.

Other problems also must be taken into consideration. People expect more than they had before the war. They expect steady employment and steady progress, and they are looking forward to great social improvement and cultural development. The Nazi occupation will leave behind it numerous grave problems. To mention but one of these, the question of changes in property initiated by the German rule will be a hard nut to crack. Hatred will have accumulated among the nations, and there may well be residua of racial propaganda. All these and many other circumstances will complicate the attainment of the economic objectives. But, however difficult it may be, it should be clear that any delay in economic reconstruction will jeopardize the progress of postwar consolidation of Europe in general.

CHAPTER TWO

CONTINENTAL EUROPE'S POSITION IN WORLD TRADE

EUROPE *can maintain her standard of living, her level of production, and the welfare of her peoples only as an integral part of a well-functioning world economy.* During the nineteenth century, continental Europe followed Great Britain as the world's workshop, importing chiefly primary products (food and feed and raw materials) and exporting manufactured articles. Europe's total economic position depends on this trade. She needs to import raw materials and foodstuffs in order to keep her industries running and her labor employed, and equally in order to maintain a standard of living that is surpassed only by that of Great Britain and North America. In spite of the fact that her relative position in world trade declined slightly, especially after the first World War, together with Great Britain she still represents the basic stone in the structure of the whole trade. Because of her dependence on world trade she is more deeply affected than the other continents by the economic, political, and social consequences of the disintegration of world economy.

In 1938, the share of the European Continent in world imports amounted to 38 per cent and in exports to 37 per cent (including Great Britain and Ireland the figures were 56 per cent and 48 per cent, respectively, of the world total).¹

¹ The figures in this chapter have been compiled chiefly from the League of Nations' publications *Europe's Trade* (1941) and *The Network of World Trade* (1942).

In the average of the three years 1935, 1937, and 1938, the total imports of the European countries amounted to \$9.71 billion; 51.8 per cent of this total or \$4.73 billion were supplied by other continents, the British Isles, and Russia. Of the total European exports during the same period, averaging \$8.06 billion, the other continents, the British Isles, and Russia purchased \$3.58 billion or 44 per cent of the total exports of the continental countries. The Continent had thus with the rest of the world an import surplus of \$1.15 billion. (The intra-European trade represented 48.2 per cent of the total imports and 56 per cent of the total exports.)

Excluding the intra-European trade from the figures of the total trade of the European countries, we obtain the following percentage shares of other continents and noncontinental Europe (the United Kingdom and Ireland) and the Soviet Union in the trade of continental Europe in 1928 and 1938 with the rest of the world:

	<i>Percentage of Imports</i>		<i>Percentage of Exports</i>	
	1928	1938	1928	1938
Africa	12	16	14	16
North America	28	23	16.5	14
Latin America	18	18.5	14	14
Asia	16	16	14	16
U.S.S.R.	4	2	2	2
Noncontinental Europe	16	18.5	36	36
Oceania	4	4	2	2

This tabulation throws into sharp relief the importance of the British market: Great Britain purchases more than one third of the goods exported from the European Continent, more than North America and Latin America together.

The following figures demonstrate the importance of conti-

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mental European trade with other continents and with Great Britain in percentage of the total trade of the areas named.

	<i>Exports to Europe</i>		<i>Imports from Europe</i>	
	1928	1938	1928	1938
Africa	43	44	54	59
North America	17	19	27	21
Latin America	30	31	35	33
Asia	15	17	19	18
U.S.S.R.	39	30	56	46
Noncontinental Europe	35	30	27	29
Oceania	11	10	33	17

Thus, even if we disregard the intra-European trade altogether, we arrive at the conclusion that continental Europe was still the most important factor in world trade, closely followed by Great Britain and the United States (which has a somewhat different trade structure).

The nine highly industrialized countries (France, Germany, Belgium, and Luxembourg, Netherlands, Switzerland, Sweden, Czechoslovakia, Austria, Italy) carry on by far the greater part of trade to and from, as well as within, Europe. These countries are important not only because of the volume of their trade but also because of its composition. Taking the average of the years 1928, 1935, 1938, this was as follows, in percentage of the total:

<i>Commodity</i>	<i>Percentage of Imports</i>	<i>Percentage of Exports</i>
Foodstuffs and live animals	24.3 (23)	12 (11)
Materials, raw or partly manufactured	51 (54)	24 (26)
Manufactured articles	24.6 (23)	63.7 (63)

NOTE: The figures in parentheses are for 1938.

The trade of the agricultural countries was to a very great extent intracontinental, comprising 75 per cent of imports (including those from the United Kingdom) and about 85 per cent of exports. In 1935 the agricultural countries accounted for only 17 per cent of the aggregate imports and for 19 per cent of the aggregate exports of all European countries. The composition of trade of the agricultural countries during the same period was quite different from that of the industrial countries.

<i>Commodity</i>	<i>Percentage of Imports</i>	<i>Percentage of Exports</i>
Foodstuffs and live animals	15.6 (13)	48 (43)
Materials, raw or partly manufactured	35 (39)	36 (39)
Manufactured articles	49 (48)	16 (18)

NOTE: The figures in parentheses are for 1938.

As a result of the upward trend in industry, population, and standard of living, Europe's need of imports of prime materials from overseas was greatly increasing. The extent to which Europe had become dependent on those imports in the years preceding the second World War is clearly seen from the data given below. Thus, she required imports of about 10 per cent of the cereals consumed in Europe, and this in spite of an increased agricultural production resulting chiefly from a policy of high protection in important industrial countries. About half of the vegetable oil and the greater part of the oilcakes used in the dairy industry had to be imported (more than one third of the total consumption of edible fats). All of the coffee, tea, and cacao came from abroad and about one third of the tobacco. In the food bracket, Europe herself was an exporter of meat, dairy

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products, and eggs (chiefly to the United Kingdom), as well as of sugar and potatoes.²

For raw materials Europe's dependence on imports was even greater, because of her deficiency in many of the basic products. She had to import nearly all the cotton and more than 70 per cent of the wool consumed, about 40 per cent of the silk, all the jute, and some flax and hemp. All the rubber came from the Far East, and South America supplied large quantities of hides and skins. While Europe was a net exporter of wood pulp, she herself imported timber, chiefly from the Soviet Union.

Shortages in the metals and minerals were also great. It was necessary to import 80 per cent of the consumption of crude copper, 50 per cent of lead, 20 per cent of zinc, 90 per cent of manganese; furthermore, by far the greater part of the nickel, tin, molybdenum, tungsten, chromium, vanadium, antimony, asbestos, mica, and cobalt were obtained from abroad, as were more than 60 per cent of the phosphates and more than 70 per cent of the petroleum used. The only raw materials Europe was able to export were potash, mercury, sulphur, gypsum, magnesite, and synthetic nitrogen.

It can be said that in nearly every phase the industrial as well as the agricultural production of the European countries was to some extent dependent on the import of raw materials, semi-manufactured products, and even some manufactures. And as the foremost importer of primary materials, the Continent had obviously achieved an important position in the market of most of these commodities.³

² The Continent imported yearly 7 to 8 million tons of food and 12 to 13 million tons of feed (the British Isles took around 12 to 13 million tons of food and 7 to 8 million tons of feed). M. K. Bennett; *Food for Postwar Europe* (Food Research Institute, Stanford, Calif., 1944), p. 11.

³ In 1938 the percentage share of continental Europe in world imports was as follows: (the figures in parentheses include the percentage share of continental

In view of the great deficit in her import of food and raw materials, it was taken for granted that Europe would have an export surplus in manufactured goods. In 1935 the import surplus in foodstuffs amounted to \$280 million, in raw materials to \$1,970 million, or a total of \$2,250 million, against which stood a surplus in the export of manufactured goods of only \$1,020 million leaving a deficit of \$1,230 million in 1935 and one of \$1,302 million in 1937.

The growing importance of Europe as a market for primary products and the dependence of several countries on this market was offset by the necessity for increased export of industrial products of Europe. This export was needed not only to obtain foreign exchange to pay for imports but equally to provide employment for the industries and labor. Though the proportion of industrial production dependent on export may seem small, we must consider not only the effects of the foreign trade multiplier on employment but also the mutual interrelation of exports in the European countries concerned.

In the four years preceding the crisis of 1930 (after which the development of foreign trade did not keep pace with the development of national production), the following percentages of manufactures were exported: from Switzerland, 37; Austria, 30; Sweden, 29.5; Czechoslovakia, 22.5; Belgium, 21.5; Germany, 20; France, 19; Netherlands, 18; Italy, 11.5. (The figure for the United States is only 4 per cent, and for the United

Europe, together with noncontinental Europe, chiefly the United Kingdom): wool, 55 (84); cotton, 48 (67); copper, 61 (79); zinc, 44 (80); lead, 35 (82); petrol, 21 (57); corn, 59 (96); wheat, 43 (83); citrus fruits, 45 (81); coffee, 41 (42); tea, 6 (59); butter, 16 (94); pork, 10 (91); rubber, 24 (36); manganese, 60 (69); tin ore, 40 (60). Of all these commodities the United States was an important buyer only for rubber (38 per cent), coffee (49 per cent), tea (9 per cent), manganese (23 per cent), and tin ore (40 per cent).

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Kingdom 27.5 per cent.) Stated simply, more than one fifth of the industrial production of the industrialized countries in Europe had to be exported in order to employ labor and provide foreign exchange. To understand the significance of this figure, we must realize that many industries work primarily for national consumption, so that, in fact, the percentage of exports in industries other than these is much higher. Although intra-European trade is included in this figure, it does not diminish the importance of export for the European economy. The basic structure on which progress in Europe has been built and its interrelation with the world economy is clearly demonstrated.

Next we turn to the question of the balance of trade and the balance of payments, in order to examine in what way Europe has paid for her needed imports. Throughout a long period, continental Europe's trade with the rest of the world has shown a great import surplus, which had to be paid for from income from other sources. This basic fact was not altered in the period following the first World War. As an example of this development we may compare the figures for 1928 (a year from a period before the outbreak of the world crisis and when international credit still functioned) and 1938 (the last year before the outbreak of the second World War). The figures represent continental European trade with the outside world.

	<i>Imports</i> (in million dollars)	<i>Exports</i> (in million dollars)
1928	6,660 (13,580)	4,760 (11,390)
1938	4,460 (9,310)	3,460 (8,060)

NOTE: Figures in parentheses include the intercontinental trade.

Thus in 1928 the import surplus amounted to \$1,900 million (old dollars) and to \$1,000 million in 1938; in 1935 it was \$1,200 million. The 1928 import surplus of the United Kingdom was

\$1,770 million, in 1935 it was \$1,356 million, and in 1938, \$1,980 million.

In the prewar years continental Europe had an import surplus with the rest of the world of more than one billion dollars. And this was during a period of a reduction in imports caused in part by decreased purchasing power but to a greater extent by various kinds of import barriers that had been erected as a result of protectionism and the lack of free foreign exchange. With all other continents Europe had an import surplus (the deficit in trade with the United States was \$890 million in 1928 and \$440 million in 1938). Her only export surplus was with the United Kingdom; it amounted in 1928 to \$898 million and by 1938 had gone down to \$565 million (in 1935 it was \$467 million).

Without this important export surplus (which averaged at least \$500 million during the years preceding the present war), the import surplus would have been substantially greater, and Europe's power to purchase abroad might well have been correspondingly lower. Through multilateral trade Europe obtained from her export to Great Britain foreign exchange that could be used to pay for imports. The "invisible items" in her international account paid for the deficit of her balance of trade. Whereas during the twenties the flow of foreign credits, especially from the United States, had financed a large part of the excess of imports, in the thirties international lending practically ceased and Europe had to rely on her own income. If it is asserted that Europe was able to do so, we should not forget that the majority of the European countries had felt obliged to introduce foreign exchange control in order to meet current payments abroad. And in spite of all these measures, "blocked foreign accounts" were not an exception but a measure to which several countries resorted.

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In analyzing the invisible items of the balance of payments, we are faced with the fact that the national statistics usually do not cite the origin or destination of these payments, thus making it very difficult to establish the European balance of payments with the rest of the world. There are, however, several known items. A number of creditor countries received income from investments in other continents, in particular, the Netherlands, France, Switzerland, and Belgium. For Switzerland, Italy, and France, the tourist traffic was an important source of revenue. In Italy, Poland, and Greece emigrant remittances, especially from the United States, totaled in good years as much as \$200 million. Shipping provided substantial income for Norway, Netherlands, Greece, and Italy.⁴ The importance of invisible items for paying the excess of imports in the past is very clear.

Continental Europe could have developed its industry, its whole economic and social structure only within the framework of an international division of production. Imports of food and raw materials were paid for, within the machinery of multilateral trade, by exports mainly of manufactured products and by invisible items in the balance of payments, that is, various services rendered or yields from foreign investments. The important role of Great Britain in this respect has already been mentioned. Should the income from invisible items decline, Europe would have to increase her exports to be able to maintain the level of imports. Otherwise, any reduction on the credit

⁴ In *Nazi Europe and World Trade* (Washington, D.C. 1941, p. 133) by Cleona Lewis, a table of a continental balance of payments for 1937 and 1929 is given, compiled mostly from the League of Nations *Balance of Payments*. In *Europe's Trade* (League of Nations, 1941, p. 31) figures are given for 1928 and 1935. Interest and dividends amounted to \$40 million in 1928 and \$290 million in 1935; services to \$2,450 million in 1928 and \$1,060 million in 1935.

side of the balance would necessarily lead to a reduction of European imports with all the attendant consequences—a decline in consumption and a strengthening of protection of national production with a tendency towards autarky.

CHAPTER THREE

EUROPEAN ECONOMY IN THE INTERWAR PERIOD

EUROPE DIVIDED

THOUGH THE TASK of maintaining trade with the other continents was Europe's great concern, other very important problems had their bearing upon the development of the European economy. During the whole interwar period Europe had never reached a real consolidation of her economic position; the only exception was the interlude in the years 1925-1930, when many countries had enjoyed "borrowed prosperity" by means of the great influx of foreign (especially American) credits. The European economy was not adjusted to the changes in the world economy already in progress before the first World War. This was, of course, due to the lack of an appropriate policy on the part of Europe as well as of the other nations. It is a matter of speculation as to what extent the unstable economic situation was caused by the equally unstable political situation, or to what extent the lack of a real economic consolidation had contributed to the political difficulties. It should be said, however, that during this period economic principles were scarcely the driving power that could have determined the course of political happenings.

The position of continental Europe in the world economy has been presented here as if Europe were a single unit. It must be underscored that this is far from the case. Continental Europe is not economically integrated nor is it homogeneous. Very often

it is represented as divided into two parts, one wealthy, and the other with a retarded economic development. Figures of national income per head, sometimes showing wide differences even between neighboring countries, easily bear out this division. In terms of international units, the annual per capita income of the working population declines from west to east, geographically, receding from 1,069 in Great Britain, 855 in Holland, 684 in France, to only 350 in Poland, 243 in Rumania, and 284 in Bulgaria. Similarly it declines from north to south; 653 in Sweden, 539 in Norway, as against 397 in Greece, and 343 in Italy. In the middle of this scale are Germany, Czechoslovakia, and Austria.¹

Most of the countries bordering on the Atlantic belong to the wealthy, well-developed area of Europe, with advanced industry and trade. These are the nations of which one may speak in terms of a capitalistic economy; they have accounted for the greatest part of the European trade. On the other hand, the most retarded regions formerly belonged to three empires—the Ottoman, the Russian, and the Austro-Hungarian. (Czechoslovakia and Austria are exceptions, in progress, in their geographical area.) The two Mediterranean nations, Italy and Spain, also remained behind the economic progress of Western and Central Europe.

The countries of Eastern and Southeastern Europe form a bloc which has several economic problems in common. In Poland Hungary, Yugoslavia, Bulgaria, Rumania, Albania, and also in Greece, the intensity of agricultural production was low, and at the same time there existed a great need for foreign markets of agricultural products. All these countries suffered from a relative overpopulation in agriculture, as the outlet of the time be-

¹ Collin Clark, *The Conditions of Economic Progress* (London, 1940).

fore 1914—mass emigration overseas—was closed. Industry was slow to develop because of lack of capital and skill and, therefore, could not provide sufficient employment for the greatly increasing population. Though this area certainly offered various good opportunities for economic development by the advanced European countries—and a consequent expansion of intra-European trade—not very much was done in this respect. Some loans were granted, particularly for stabilization purposes; British, French, Czechoslovak, and other concerns contributed to the development of natural resources and industry; but there was no systematic or comprehensive attempt to work toward the economic advancement of this politically vital part of Europe. And only by such a policy could a successive narrowing of the great differences in the economies of the two parts of Europe be achieved and a better integration of the European economy be prepared.

It is only natural that, when in 1930 the world economic crisis broke out, this backward part of Europe was the one to be hardest hit. It should have been clear to the leading powers that, unless a really constructive solution was worked out, the crisis would lead to new political developments. At that time, however, Germany's political weight had increased and she had renewed her claim that Southeastern Europe be considered an area of her special economic interests (later called her *Lebensraum*). In the West, Germany found a resounding platform for her claim. Often it was pointed out that, whereas the Western powers do not provide any substantial market for the agricultural export of the Danubian basin, Germany is the natural customer of this part of Europe, and it is logical that the role there be more eminent.

Thus Germany, using all the now well-known devices of the

so-called Schacht plan, started a well-planned trade penetration in Southeastern Europe. Using the methods of bilateral trade and clearing agreements, which practically amounted to a barter system, she succeeded in detaching the Danubian agricultural countries from the world economy, and step by step drew them into her armed economy. After the annexation of Austria and the occupation of Czechoslovakia she completely dominated the foreign trade of the five agricultural countries in Southeastern Europe, absorbing more than half of their aggregate trade. As a matter of interest it should be mentioned that the British policy—based on the Ottawa agreement to buy an increasing amount of agricultural products within the British Commonwealth—and a similar French policy had not made the position of the European agricultural countries easier.

ECONOMIC NATIONALISM

Thus, instead of progressing toward integration, the economy of the Continent before the second World War was divided not only into wealthy and retarded areas but also into two different trading systems. One of the groups of countries was under the influence of the German commercial policy based on bilateral trade and expanding government control of all business transactions. This group included practically all countries east and southeast of Germany and also included Italy. Czechoslovakia and, to a lesser extent, Poland and Austria, attempted to escape this bilateral trading system and to maintain multilateral trade with the Western world. However, the system of bilateral trade was spreading even to Western Europe, where some of the countries, Great Britain not excluded, concluded payment agreements also. Nevertheless, on the whole the advanced Western countries made great efforts to maintain the multilateral net-

work of world trade. As a result first of the world economic crisis and later of the armament program introduced in many countries, *economic nationalism* was strengthened. Certainly, continental Europe could point to the high tariff policy of the United States, which was only slightly moderated with regard to manufactured goods by the trade agreement program started in 1934, and also to the fact that even Great Britain had felt it necessary to reverse her old free trade policy and to introduce in 1931–1932 a general tariff protection and to organize a system of imperial preferences. In most continental countries, however, the policy of protection was not confined to high tariffs; all kinds of quantitative foreign trade restrictions were resorted to—general import permit systems, quotas, foreign exchange restrictions, and clearing agreements. These, together with various devices of administrative protection, have all become weapons of the foreign trade policy arsenal. The policy of self-sufficiency, strongest in Germany and Italy, gained new support when in several countries the necessity for it was emphasized in connection with the armament program and the national defense in general. Supported by the high waves of political nationalism, great parts of Europe plunged into a policy of *economic ultra-nationalism*.

It is small wonder, therefore, that a real expansion of intra-European trade did not occur. Instead, the industrialized countries, under a high protective tariff, and sometimes with the aid of a complete government monopoly, increased agricultural production, reduced agricultural imports, and, in consequence, lost their export of manufactured goods to the agricultural countries. At the same time, the industrial countries created new industries and protected the existing ones, because this was considered necessary to reduce unemployment. Similarly, the agricultural countries, especially those of Eastern Europe, also

under a most complete protection (and without regard to the cost of production and of prices abroad) stimulated the erection of new industries. Thus the cleavage in the level of prices steadily increased; in industrial Europe (with the exception of the Low Countries and the Scandinavian countries) prices of agricultural staples were much higher than those in the world markets or even, in some cases, than those in the agricultural, sometimes neighboring, countries of Europe. Obviously, Germany led in this high level of agricultural prices. Meanwhile, the peasants of the poorer areas of Europe were paying very high prices for domestic manufactured goods.

In spite of the fact that in several countries production was increased under the direct or indirect influence of the armament programs, Germany alone succeeded in eliminating unemployment. As we know, this was achieved only by setting up an armed economy in peacetime. Even in 1937 relatively high figures of unemployment could be found in Austria, Belgium, Denmark (21.9 per cent of the total number of workers); France, Czechoslovakia, Norway (20 per cent), Netherlands (29.2 per cent), and Switzerland. Only in Sweden and Great Britain were the figures lower. Thus, even during a period of greater employment initiated by the armament program and public works, *the policy of protection could not make up for the lack of expanding and orderly working multilateral trade in the world.*

During this period the situation of the Danubian agricultural countries seemingly improved. This was chiefly due to the German policy of buying all available or proffered supplies of raw materials and most of the foodstuffs, but it resulted in absorption of the area into the German economic system and isolation from the world markets. As a consequence, economic independ-

ence was the first to be jeopardized, and soon afterwards political independence; furthermore, none of the major economic problems of the area were settled.

GOVERNMENT INTERVENTION

Throughout Europe the growing economic difficulties led to a greater *emphasis on the government's role in economic life*. Even before 1914 government intervention on the Continent was greater than in the Anglo-Saxon countries. In the eighties of the last century liberal capitalism in Germany and in Austria-Hungary had been succeeded by a policy of benevolent intervention. Only in the Low Countries, Switzerland, the Scandinavian countries, and France had economic liberalism set firm roots. In Germany and the countries east of Germany, political and social remnants of feudalism still contributed to the rather strong position of the civil servants. Moreover, the importance of economic liberalism and capitalism was interrelated with the strength of the middle class. In the backward agricultural countries the middle class had never been strong; in Germany and in some of the other countries its position had been greatly weakened by the postwar inflation.

From 1930, in almost all of the countries government interference with economic life was on the increase. The new role of government put parliamentary democracy to a heavy trial. In most of the European countries there were numerous political parties, often organized along the line of special economic and social interests—something which might be called pressure-group representation. Compared with these, the all-national parties which emphasized the patriotic duty of all citizens as against special interests were in the minority. Nowhere was parliamentary democracy prepared or equipped to cope with

the new task. Its failure caused great disappointment; the confidence of large masses of the people was lost. The notion of economic freedom was usually interpreted as protection against the influence of big business and capital. Very seldom was it realized that real economic freedom may also be menaced by government control of economic life. This is particularly true when the government does not limit its activity to the general program planning—to issuing directives for the economic policy in general—but takes it upon itself to regulate everyday business transactions.

Under these circumstances the position of the civil servants of an economic bureaucracy had become extremely important. Not only in the totalitarian countries but in all nations where government intervention in business transactions (foreign or domestic) was expanding, the role and importance of bureaucracy was growing. The same Europe which only a hundred years ago had freed herself from the often uncontrolled power of bureaucracy with regard to political rights (mostly under absolute monarchs) and had organized a system of protected political freedom coupled with legal security and justice was now slipping back unnoticed into another kind of often uncontrolled bureaucracy extending the public control over steadily growing areas of economic life. The problem of freedom, of democracy, and controlled economy was opened on a broad front.

The system of private enterprise still prevailed throughout Europe. Although the governments and other public bodies owned railways, communications (and, in some countries, forestry, mines, mortgage banks, savings banks and armament factories), the great bulk of industrial as well as agricultural production was owned and managed privately. Even Nazi Germany had not nationalized any important private enterprises.

Nevertheless, the real scope of free initiative was steadily reduced by all kinds of government control. The whole economy had become less flexible and had lost much of its dynamic character. It could hardly be otherwise in countries where good political relations were sometimes of greater value to the entrepreneur than efficiency and skill. Again, in the Western countries along the Atlantic border greater freedom prevailed and more understanding was shown in relation to private enterprise than in the rest of the continent.

Except in Germany (and to a lesser degree in Italy), where the preparation for war had determined the whole course of economic policy, it is not easy to determine the guiding principles and objectives of government intervention. Certainly, it has not succeeded in working out an economic system capable of providing employment, of increasing national production, of smoothing out differences among the various economic and social interests; nor has it built a basis for the confidence that is so important to the success of any private or public economic program.

Throughout the whole interwar period *the social problems*, especially the relation between labor and capital, remained in the foreground of public interest. In most of the industrialized countries the position of labor had improved. The system of social insurance and other social legislation was expanded and ameliorated, although in some countries (for instance in France) the conservative circles were slow to realize the necessity of providing this kind of social security for labor. In other countries (as for instance Sweden and Czechoslovakia), a comprehensive system of social insurance was introduced in the early postwar period; in most points this approached the objectives of the Beveridge plan of 1943.

In general, the level of real wages and labor's share in the total national income had increased. In spite of this improvement, no real or consistent political cooperation between labor and capital could be relied upon, a fact which proved particularly unfortunate when the unemployment figures climbed up during the thirties. It would have been extremely helpful if a united front had been presented by all people engaged in production.

The political parties representing labor were largely dissatisfied with the achievements in the field of social legislation and with the improvement in the level of living, a matter which obviously became very difficult during the time of the deep depression. On both sides, the issues were broad. Labor complained that, although politically a very powerful factor, it had no possibility of taking part in the important decisions regarding private enterprise, and it accused capital of using indirect methods to influence political issues. Capital, on the other hand, obviously numerically weaker in its political representation, pointed out that, although it had to bear full responsibility for important questions of national economy, it had little to say in matters of political decisions which vitally affected the economic life.

In a number of countries the socialist parties held up the class-struggle concept, and frequently they still followed the Marxian doctrine in their economic program. A genuinely constructive economic program embracing the interests of the whole national economy was seldom a part of the policy of the socialist parties. One feature common, perhaps, to a majority of them was an emphasis upon the problem of better distribution of national income rather than improvement of the standard of living by a general increase in national production. In relatively poor countries, especially, the latter course was certainly the only constructive method to adopt. Surprisingly little interest was shown

by the socialist parties in the importance of expanding foreign trade, which could obviously only be achieved by a policy of freer trade.

Capital and industry, remaining mostly on the defensive, considered themselves equally menaced by the growing government control of business and by the policy of the socialist parties. They, too, were very slow in presenting a constructive program or in taking the offensive even where the situation called for it. The demand for a radical change in foreign trade policy was seldom heard from them. In some countries, short-sighted leaders of industry hoped that by supporting fascism they might find assistance against the menace from the left. The fear of communism played an important part in this. They did not realize, of course, that for a seemingly greater safety from the dangers of nationalization they would have to submit to a complete economic control, to a regimentation carried out by totalitarian regimes.

But even labor was not unreceptive to the promises of a better life and a guaranteed job in a totalitarian state. How else may we explain the quick acquiescence of German labor, of the strong German socialist parties, to the Nazi regime? During a period of mass unemployment the prospect of economic security loomed brighter than that of freedom.

Thus the picture of the economic and social situation and political constellation of Europe before the second World War was certainly not cheerful. In an unstable world economy in which the postwar maladjustments had not yet been corrected, the position of Europe had grown relatively weaker. To these difficulties the effects of a strong economic nationalism on intra-continental trade must be added. In the process of the economic

integration of Europe very little progress had been made; she remained divided into advanced and backward regions.

Expanding government intervention in the economic sphere, which hardly followed any constructive pattern, often proved a very disturbing element. The mixed economy put a brake on private initiative for which no compensation was offered by proper measures in the sphere of public economic activity. The dynamic economic forces were slowed down. The social struggle that remained beneath the surface throughout the major part of the period also contributed to the economic uncertainty and often paralyzed the determination of the more active forces in the respective national economies. The high waves of nationalism and later on of racism—especially the anti-Semitic tendencies that spread from Germany to a number of countries—further aggravated the complex situation. It can be said that generally the real economic issues were overshadowed by the national, political, social, and racial problems and later on, decisively, by military considerations. Nevertheless, in spite of all the obstacles, the national economies of Europe achieved some progress and did not cease to struggle for higher employment and technological advancement. This fact certainly speaks well for the inherited strength of the European economic structure and for the efficiency, devotion, and stubbornness of the men who were actively engaged in performing their tasks in economic life.

CHAPTER FOUR

THE IMPACT OF THE WAR AND OF THE GERMAN DOMINATION

ORGANIZATION OF PRODUCTION FOR WAR

ALTHOUGH it is still too early to evaluate completely the impact of war and German domination on the economy of the European countries, nevertheless we have sufficient data to enable us to make some assumptions and to arrive at several conclusions. The economy of all the occupied countries in Europe, and to some degree even of the few which remained neutral, was directed by Berlin. The uniform German plan aimed not only at harnessing all economic resources for the support of war but also at a long-range objective. According to this program Europe was to be organized into one economic and political unit headed by Germany—which in this way would have gained permanent domination. Europe was to become independent of the outside world in respect to foodstuffs and indispensable industrial materials in order to be freed to a large extent from dependence on the world market and from the influence of world business cycles.¹ The Germans argued that only on the assured basis of a United Europe could a really fruitful exchange in foodstuffs, raw materials, and industrial goods be developed. To attain autarky it would also be necessary to bring all agriculture up to the German level. In such a completely controlled economy the problem of unemployment would be solved. This program was the blueprint of the Nazi

¹ See the author's *The New Economic Warfare* (New York, 1941), pp. 155 ff.

"New Order," and was to have been carried out even during the war. The course of the war has, of course, changed the German intention, and the requirements of a war economy made it impossible to go ahead with various parts of the whole program, although some of its features were put into operation.

Two aspects of the New Order were much emphasized and—at least for a while—achieved some success in propaganda. The one was the assurance of employment and the elimination of the cyclic fluctuations; the other was the stress laid on the self-sufficiency of Europe which promised a larger continental market and a speedy advancement of the retarded agricultural countries. It has been stated repeatedly that even without foreign trade with the overseas countries full employment has been achieved and can be permanently assured, thereby reducing the dependence of Europe on the rest of the world. At what cost and sacrifices this can be done has, of course, not been questioned, because cost is of minor importance in a war economy. And German experts have refuted the consideration of comparative costs by pointing toward a full and assured employment.

Fortunately, Germany did not have time to carry out the blueprint of the New Order. To examine today the economic weakness of the whole plan—even leaving aside the basic political question of the German domination over the other nations—would only be an *ex post* analysis. Yet it is not impossible that some of its features, in so far as they suit various groups, may be brought forward again in the future.

During the war the economy of the whole continent was obviously harnessed for one purpose—to fill the needs of the German war machinery. The conversion from peace to war production went further in Germany and in the occupied coun-

tries than anywhere else. As manpower and raw material shortages increased, production of all other than military goods was steadily curtailed. The system of maximum exploitation of labor that was established in the occupied countries by a decree of August 22, 1942, introduced the following order of priority for the use of manpower: 1) the army of the occupation authorities and civil authorities; 2) the German armament industry; 3) food supply and agriculture; 4) industry in the German interest outside the armament industries; 5) industry in the interests of the population of the territory in question. A minimum output was allowed for civilian consumption—only what was urgently needed for bare existence or for maintenance of the necessary morale.

Manpower was not only shifted from factory to factory, but, in the course of a combing-out process, employees in trade, banking, civil service, and in liberal professions were sent to factories. Labor was moved wherever it was considered necessary; about eight million foreign workers were sent to Germany. By all these and similar measures the Germans weakened the position of the middle class in the occupied countries, while attempting at the same time to improve, at least seemingly, the situation of labor.

A particular feature of the German war economy is the wide use of substitutes, growing out of the lack of raw materials. Production of substitutes (*Ersatz*) and also of new materials was particularly notable in oil, synthetic rubber, synthetic fibers, and all kinds of plastics. Manufacture of these was not limited to Germany but was also organized in some occupied countries, chiefly for military reasons. In Austria, Czechoslovakia, and Poland many such plants were established, and even in Western Europe production of, for instance, synthetic fibers and arti-

ficial substitutes for fodder (for example, *Futterhefe*) was increased. It is clear that the production of substitutes further intensified shortages of labor and of coal.

This particular aspect of the German war economy has one important consequence. Whereas in the United States and other places research and technological progress continued on the established basis and achieved many remarkable results, in Europe such technological progress stopped and respective relations with the outside world ceased. At the close of the war European industry will not be on the level of the progress achieved by various industries elsewhere, especially in the United States. On the other hand, it is to be expected that in the manufacture of so-called new materials, as plastics, great progress will have been made and, furthermore, that many new uses for light metals, the production of which has been greatly expanded, will have been found. After the first World War wide use was made of the technical achievements of the war; it is very likely that this time even more of the new methods will be found useful and even greater progress will be witnessed in their application to peacetime production.²

The production of substitutes and the strategic moving of industries from Germany to Eastern Europe may result in increased industrial production in the agricultural countries. While it was German policy to discourage all industries considered nonessential for her own ends, she supported some key industries outside the Reich, and also developed metallurgical resources in some other countries to furnish substitutes for the metals Europe lacks. Deposits of low-grade iron, copper, and tin were exploited and water-power installations were expanded.

² See Cecil H. Desch, *Substitute Materials in War and Peace* (London, 1943), and *Occupied Europe* (London, 1944), pp. 68 ff.

In the field of agriculture the Germans have in their own interest initiated certain improvements in organization. (These were not always a success.) One of the important items of the German plan was to increase production of oilseeds, not only in Southeastern Europe and in Germany, but also in France and in the Low Countries. Here the oilseed area rose from 50,000 hectares in 1939 to some 250,000 hectares in 1943. The Hungarian sunflower and rapeseed area rose from 18,411 ha. in 1939 to 130,000 ha. in 1942, while the Bulgarian sunflower and soybean area rose from 232,000 ha. in 1938 to 270,000 ha. in 1942. The Western countries which had depended on imported fodder were forced to grow more cereals. All over Europe the acreage under cereals, root crops and oilseeds had been increasing.³

It still remains to be seen how much of the new industrial production of the agricultural countries, especially, and how much of the various attempts to improve agriculture will be of durable value. One factor, however, should remain in any case; namely, the greater skill of labor. Workers who were sent to Germany as well as those placed in newly organized manufactures at home were bound to acquire new experiences and greater skill—a useful asset in the future development of industries in the retarded countries.

³ Even in Switzerland the oilseed area increased from 178 to 1,212 ha. between 1940 and 1942 and, in Sweden, from 20,028 acres to 64,296 acres between 1941 and 1943.—M. K. Bennett, *Food for Postwar Europe* (Stanford, Calif., 1944), p. 39.

In a recent article ("European Agriculture," *Foreign Affairs*, Jan., 1945, pp. 288–289) Karl Brandt made the statement that it would be a serious mistake to ignore the unpleasant fact that Europe's agriculture has been successfully operating within the consolidated market of the Fortress. See also Karl Brandt, *The Reconstruction of World Agriculture* (New York, 1945), pp. 133 ff. This book was published while the present study was already in press; it was not possible, therefore, to make extensive use of it.

Nevertheless, it should be emphasized that whatever was done resulted from the deliberate and ruthless German policy of domination and enslavement. Within the occupied countries independent economic life ceased to exist, and national economies were disintegrated to the point of a breakdown. It is necessary to realize the enormous degree of regimentation which took place in the economic life of Europe. In Germany and all countries under its rule economic life was regimented in minute detail. Government agencies dictated what to produce, at what prices to sell, whom to employ, what wages to pay, and what profit to distribute. Prices and wages were fixed, labor conscripted and allocated. For every new investment, for repairs, and for the use of idle funds, government permission was needed. These restrictions have gone far beyond the wartime economic regulations of the democratic nations. The same thing applies to foreign trade. On the whole, a completely regulated totalitarian economy was introduced. The system of private ownership was maintained by the Germans at home as well as in the occupied countries. The function of entrepreneur, however, became that of a quasi-government agent who held his position only with the consent of the German authorities with whose directives he must comply. The functions of private enterprise have been reduced to maintaining title to ownership without the possibility of exercising any of the established rights and activities. Private enterprise has been emasculated.

ECONOMIC AND FINANCIAL EXPLOITATION

The financial structure of the European countries under German rule has been disrupted and disorganized. Germany herself tried desperately to avoid inflation, the memory of which was still alive in the minds of the German people. Using drastic

measures, she succeeded in meeting about 45 per cent of her total expenditures by taxes and contributions from the occupied countries and the rest by borrowing chiefly on short-term loans. As a matter of fact, this procedure had become compulsory borrowing, although this was not legally stated. All kinds of devices were employed to syphon off the excess purchasing power. By a very strict regulation of prices and income, and by means of rationing, the price level was held down. Judging from the official price indices, Germany experienced the smallest price increase of all the belligerent countries; however, inflation on a large scale is to be expected before the end of hostilities.

Germany extorted from the occupied countries large contributions in several forms. At the end of September, 1943, total contributions from occupation costs amounted to about Rm. 42.8 billion, and the annual rate of payment was roughly equivalent to Rm. 16 billion. Moreover, in return for their goods and services, the occupied countries had, to a great extent, to accept credits on clearing accounts with Germany, instead of using these to buy the goods they themselves needed to import. All clearings were operated through Berlin, and Germany accumulated a huge clearing debt. She took all the goods she could get and deferred payment wherever possible. The clearing debt was considered as a long-term noninterest-bearing loan to be paid after the war in terms to be imposed by Germany. By the end of September, 1943, Germany's total clearing debt reached about Rm. 21 billion; the countries occupied at that time alone accounted for some Rm. 18 billion; the annual rate of increase for these countries was estimated at Rm. 6.75 billion. Occupation costs and the clearing debt with the occupied countries taken together amounted to over Rm. 60 billion (about \$18 billion), or a greater amount than all Germany's reparation pay-

ments after the last war.⁴ (The annual burden equals nearly one fifth of Germany's annual war expenditure.) To all this must be added the value of the property seized by Germany, and expenditures in German currency or in occupation currency.

The contributions of the occupied countries to Germany led to a credit expansion on the part of the central banks and to an increase of the note circulation, and were of a highly inflationary character. At the same time there was an increasing shortage of goods.⁵ Germany hoped to achieve in the occupied countries an internal price stability similar to her own. This succeeded only to a certain extent, varying in different countries. The high occupation costs and the mounting clearing debts, together with the declining supply of goods made the stabilization of prices on the German standard impossible to achieve. The Germans have not received the cooperation of the people, and even high penalties failed to curb the black market.

In the agricultural countries of Southeastern Europe the rise in prices was greatest. The index of wholesale prices from June,

⁴ *Occupied Europe*, pp. 34, 35. Thirteenth Annual Report of the Bank for International Settlements in Basel, p. 153. This report states on page 29: "In Europe clearings have largely ceased to serve their original purpose of equalizing incoming and outgoing foreign payments and have become a credit device by which a government advances the funds necessary to enable its country's export to continue even when no adequate countervalue is obtained from the importing country."

⁵ The increase of the note circulation is illustrated by the following table from the Thirteenth Annual Report of the Bank for International Settlements, p. 303:

Basis, January-June, 1939 = 100

<i>June, 1943</i>		<i>June, 1943</i>	
Greece	5,382 (March, 1943)	Belgium	337
Bulgaria	662 (December, 1942)	Germany	322
Finland	415	Holland	252
Italy	450	Portugal	269
Hungary	370	Denmark	245
France	364	Switzerland	154
Rumania	327	Norway	397

1939, to December, 1942, increased by these percentages: Bulgaria, 101; Hungary, 88; Rumania, 252 (retail prices); Yugoslavia (cost of living), 364; France, 145 (249 in 1943); Denmark, 95; Finland, 127; Norway, 79 (176 in 1943); Sweden, 79; Switzerland, 103. In general, it is difficult to measure the increase of price levels in view of the unknown extent of black-market operations and because it is nearly impossible to compare present price indices with prewar indices. Not only has the quality of many goods deteriorated but the official list frequently indicates commodities no longer available. The experience gained in Italy, France, and of course in Greece has shown how premature it would be to evaluate price levels on the basis of official indices. It is certain that in all these countries the long-established relations between price and cost were disrupted; no such thing as market prices exists. Moreover, the price system has been entirely isolated from the international markets, and it will be some time before we can expect a more regular price structure.

In the first place, in Germany—and to an even greater degree in the occupied countries—a latent inflation exists. The high incomes of the war period, in so far as these have not been taxed off or invested in long-term loans, are at present immobilized. Despite a strong tendency to invest money in some “tangible values,” the lack of goods and the system of rationing prevented people from spending. Savings deposits and the liquid funds of business enterprises have greatly increased; the banks show a substantial rise of deposits and it can be assumed that large amounts of money have been hoarded. However, in many countries 70–80 per cent of the assets of the banks and savings banks are covered by government bonds, and, in some countries, by claims against the German government.

The fate of savings, social insurance, and life insurance funds will be an important problem in France, Czechoslovakia, Austria, Italy, Germany, and elsewhere. The loss of savings after the first World War definitely weakened the social balance and structure in many countries. Should such a loss be permitted twice in one generation? This will be only one of the problems to confront European governments in the course of establishing orderly monetary regimes. In several countries the situation will be extremely difficult. In Yugoslavia, where six different monetary systems have been imposed, six different currencies have been in circulation; there are four in Czechoslovakia and three in Poland. In Greece the monetary system has been completely disorganized.⁶

The gold of the occupied countries that was not sent abroad for safekeeping and the foreign assets that were not held in Allied countries were depleted by the Germans. All these countries will be faced with the danger that the potential inflation may flare into open inflation. If the whole money structure is not to be ruined, quick determined action must be taken. The experience in the liberated countries has shown already that it is necessary to maintain a comprehensive system of price control and rationing and to combat the development of black markets of any kind. Of course, the real remedy lies in supplies from abroad and an increase of domestic production, assuming an appropriate monetary and fiscal policy. The experiences following the last war may be to some extent helpful.

Furthermore, the economy of the occupied countries has been subject to another important German act of force, namely the

⁶ A provisory stabilization of the Greek currency has been introduced on the basis of one pound (sterling) to 600 new drachmas, a new drachma being just equal to 50,000 million old drachmas.

changes in ownership of property, particularly of business enterprises. These changes were carried out on a large scale as a part of the German policy to achieve complete domination over all the important industries of Europe. A systematic penetration of the several national economies was made in order to control all important means of production. From the very beginning the Germans have endeavored to create such a complex situation as to prevent restoration of the *status quo*. Their penetration technique has been flexible enough to permit adjustment to local circumstances.⁷ One point is emphasized in all their manipulations, that is to provide an element of legality: Anti-Jewish measures were the first instrument in acquiring important property; yet very soon the Germans seized or "bought" other property, using various reasons and employing the necessary pressure. In the Western countries they concentrated, at least in the beginning, on utilization of existing facilities under what might be called "normal financial practice." In Central and South-eastern Europe, including the once satellite states and the Protectorate of Bohemia and Moravia, practically the whole economic life has been absorbed. In Poland, Yugoslavia, and the Baltic states the penetration has been described as "the robbery of a great quantity of industrial and commercial enterprises without any compensation."⁸ With the progress of war and the increased brutality of occupation, the depredations have steadily mounted. Throughout the continent Germans have acquired important economic positions, and in most of the countries they have succeeded in dominating the leading industries and banking enterprises. The value of this property can certainly be

⁷ See the author's *Industrial Property in Europe* (New York, 1944) and *Germany's Economic Conquest of Czechoslovakia* (Chicago, 1941).

⁸ United Nations Information Office, *The Penetration of German Capital in Europe* (New York, 1943), p. 5; F. Munk, *Legacy of Nazism* (New York, 1943).

estimated at several billion dollars. All this was part of the overall plan to make Berlin the controlling center of the European economy.

It seems necessary to emphasize here, that, whereas the Germans have gained enormous property holdings in Europe, no real export of capital from Germany has taken place to pay for all this new wealth. A great part of the property has been confiscated without any payment to the rightful owner. In many cases of a "voluntary deal" the owner received but a small fraction of the real value. And, whenever the Germans have made payment, the means were as a rule provided from the resources of the country to whose nationals the payment was made. These changes of property, which occurred in unprecedented volume and were of a revolutionary character, were more extensive in Central and Eastern Europe than in Western Europe.

It is clear beyond any dispute that German ownership, secured during the period of domination, will not be recognized by any of the countries concerned. The London Declaration of the United Nations on January 5, 1943, is very definite on this point: the states concerned reserve the right to declare invalid any transfer of property and of rights which are or have been situated in territories which have come under the occupation or control of the enemy. Nevertheless, when liberation occurs, disentangling this complex situation will be no easy task, particularly if the property has passed into the hands of nationals of an occupied country. (This was often the case as a result of a forced "Aryanization" of business.) It should be understood that decisions with regard to property of business enterprises acquired as a result of German influence will greatly affect the political, social, economic, and moral situation in many European countries.

Not only have the Germans acquired ownership or control of industry and banks, but they also exercise control over the industry in all occupied countries by means of compulsory cartels and the allocation of raw materials. In many cases goods formerly made wholly in one occupied country were later produced in a series of processes only some of which were carried out in the factory originally manufacturing the whole product, other processes often being completed in Germany.⁹

As far as we can determine today, the balance sheet of continental economy does not lead to optimistic conclusions. In contrast to other continents, the really productive capacity of European industry has not been increased. A great number of factories will have been destroyed or greatly damaged; machines will be worn out, and many spare parts and tools will be lacking. Many factories that produced peacetime goods have been dismantled. There will be little stock of raw materials of any kind and none at all of those imported from overseas. Agricultural production, suffering from lack of fertilizers, machinery, and manpower, declined in spite of all attempts to reach higher yields and its position will be far worse than it was at the end of the last war.¹⁰ Livestock has been depleted. Milk production is believed to have fallen off perhaps one third. In most countries railway stock has been greatly reduced, and the upkeep of rail-

⁹ There has been some standardization of Europe's manufacturing capacity, particularly in the engineering, textile, and chemical industries. Much of the valuable industrial specialization of some countries has been sacrificed to the needs of Germany's war industry. These wartime relations will end with the war and new specializations and integrations will have to be worked out.

¹⁰ As stated in *Food for Europe after Victory* (National Planning Association, Washington, D.C., 1944), p. 13, Nazi Europe ate less than half as many eggs as prewar Europe, 40-50 per cent less milk, fats and oils, and about a third less meat and cheese. The consumption of potatoes and fresh vegetables has increased greatly. It has been reported that in Belgium the number of cattle was reduced by about one sixth.

ways neglected. The same applies to public utilities. Added to all this is the disorganization of the financial structure and monetary systems and the fact that government interference with economic life has reached the stage of a complete regimentation and commandeering. The position of the urban middle class has been weakened, and the social balance is in danger of upset.

Furthermore, as the established commercial and technical relations with the rest of the world were cut off, one by one, a preponderate share of the foreign trade of all European countries was routed to Germany.

UNIFICATION OF THE CONTINENTAL ECONOMY?

It has been suggested by some experts in Great Britain and the United States that the German economic domination of the continent would at least have the effect of unifying Europe's economy and that this unification, now being utilized for war purposes, contains some valuable elements which should be retained after the war. Few will be found to hold this opinion now. The Nazification of Europe was not intended to produce an economically integrated Europe, the objective of the German policy was to organize Europe for the maximum benefit of the German race. As stated by the Reichsminister of Economics, Dr. Funk, in 1940, "The peacetime economy must guarantee to the greater German Reich a maximum security and to the German people a maximum of consumption of goods in order to increase their welfare. Europe's economies must be directed toward this end." There was no free trade between Germany and the other parts of Europe—except the so-called incorporated areas and Holland—and, therefore, there was no real mechanism for price and cost adjustment. The only uniformity achieved or even at-

tempted was designed to adapt all the economies to supplying armaments, food, and raw materials for German war requirements. No real economic integration of Europe could be expected from the German domination, which, as its aftermath, leaves a further disintegration of the European economies. Indeed, it would be difficult to quote a single example of integration, which, judged by peacetime standards, would be useful.¹¹

From what has been said, it can be deduced that the war has not changed the basic structure of the European economy and that its future welfare will depend to a great degree on trade with the rest of the world. The policy of autarky has hardly supplied any convincing arguments in favor of the greater independence and self-sufficiency of the European continent. Some might argue that the blockade, the cutting off of Europe from overseas supplies, has not proved to be very successful in defeating Germany; the great hopes in this weapon which were raised at the beginning of the war were decidedly not fulfilled. There can be no doubt that the economic preparation of Germany for war made her less vulnerable against blockade; we know, for instance, how greatly her self-sufficiency in food was increased. On the other hand, it is true that throughout the better part of the war the blockade was never fully effective. There were great loopholes through which Germany obtained goods: until 1943, she was able to get important materials from the invaded parts of Russia; until November, 1942, she was supplied with important goods from French North and West Africa, and until 1944 from Turkey. Moreover, she had accumulated huge stocks. Finally, a vastly enlarged production

¹¹ "Surely the common exploitation of a number of European countries during the war is completely different from a natural integration and extended division of labor for peacetime purposes," says Kurt Getz-Wold in "International Aspects of Norwegian Economic Reconstruction," *International Affairs*, XLIV (1944), 65.

of substitutes and new materials enabled her to carry on. (It is estimated that the production of substitutes alone required about one third of the total output of electricity in Germany.) Economic considerations being wholly disregarded in wartime, it was merely a question of how much of these materials could be produced; no peacetime economy could have borne the burden of production of substitutes to replace goods available through the usual channels of international trade. However great the expansion of new and old production was, it could not have supplied the needs of the population. Drastically reduced consumption of civilian goods and using up the substance were symptoms of the situation.

It is true that by adjusting production and consumption the Continent managed without importing grain from overseas, but the adjustment was made "at the price of turning the dietary clock back two generations in the industrialized nations."¹²

The cardinal question of the future will be how the impoverished population of Europe can attain a standard of living even similar to that before the war. But the people in Europe will demand more: they will ask for something better than the prewar standard and for a satisfactorily high level of employment. What social and economic policies will be devised to meet these objectives? What will Europe's position be in the changing world? How will she fit into a new equilibrium of the world economy? The changes in the economic and financial position of Great Britain as well as the new economic development of the overseas countries indicate the extent of the readjustment that European production must make.

¹² Karl Brandt, *The Reconstruction of World Agriculture*, p. 362.

CHAPTER FIVE

GREAT BRITAIN AND CONTINENTAL EUROPE

GREAT BRITAIN has been the greatest single purchaser of European exports. That this remained true even after she had established a more comprehensive system of protective tariffs is largely due to the fact that foreign exchange restrictions were not introduced, duties remained moderate, and quantitative import restrictions were applied only in a comparatively limited degree. By most of the European nations Britain was considered the only relatively free market where it was still possible to sell goods under competitive conditions. She offered market possibilities for practically all kinds of goods. In 1938 Great Britain took the following proportions of the export of European industrial countries: from Sweden, 24 per cent; Netherlands, 22.7 per cent; Switzerland, 11; Czechoslovakia, 9; Austria, 5; Belgium-Luxembourg, 14; Germany, 10; Italy, 5; France, 11.

The British market was of the utmost importance for animal products and fruits. Nearly a third of the imports of meat, eggs, cheese, processed milk, and butter came from the European Continent, the animal fats, to a considerable extent, from the nearby Lowlands and from Denmark, Sweden, Poland, and the Baltic States.¹ Even after the preferential treaties with the British Dominions were introduced in 1932, the European countries

¹ During the prewar years the United Kingdom imported 92 per cent of its butter, lard, and raw materials for margarine, 81 per cent of its bacon and ham, 69 per cent of its cheese, and 11 per cent of its cream. Karl Brandt, *Fats and Oils in the War* (Stanford, Calif., 1944), p. 37.

continued to send large supplies of these products to Great Britain.²

Among the agricultural countries Denmark ranks first in trade with Great Britain, sending around 55 per cent of her exports to that market. The figures for the other agricultural countries are: Finland, 45 per cent; Latvia, 43; Lithuania, 39; Estonia, 39. Spain sent 22 per cent of her export to Great Britain, Norway, 28, and Portugal, 21; whereas Great Britain took only about 8 per cent of the total export of all the agricultural countries of Southeastern Europe.

Although the role of Britain in the export of the European countries varies—being most important for the Scandinavian and Baltic countries, and considerable for the Low Countries, France, Spain, and Portugal—indirectly or directly, it has been a weighty factor in the economic situation of Europe. Its importance increased particularly during the period of exchange restrictions, when several countries urgently needed to get payment in free exchange in order to buy the necessary commodities from overseas. Great Britain not only paid in free exchange, but she still had a large import surplus with most of the European countries. In 1938 this amounted for industrial Europe (excluding Sweden) to \$249 million, for the Scandinavian and Baltic states to \$274 million, and for the rest of Europe to \$48 million, or \$571 million for the whole of Europe.³ It is true that Great Britain had also credit items in her balance with Europe from shipping and other services and from her investments. The investments, of which a great part were in Germany, totaled

² In the period 1929–1931, 83 per cent of the imports of bacon and ham came from Europe as against 5.7 per cent from the British countries; in the years 1936–1938 the share of the British countries rose to 27.6 per cent while the share of Europe fell to 67.5 per cent.

³ League of Nations, *Europe's Trade* (Geneva, 1941), p. 40.

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only about \$1,000 million (£225 million) and yielded not more than 3.5 per cent (£8 million). On the other hand, there was an important revenue from the tourist traffic and some other “invisible items” among the debit items of the British balance of payments.

It can be assumed that the balance of payments between Great Britain and the Continent showed a large surplus for the European countries, and provided them with foreign exchange, especially with dollars, needed for the payment of overseas imports. Europe's trade with Great Britain formed a part of the multilateral network of world trade; it certainly was a substantial factor in Europe's trade with other continents. The great changes which occurred in Britain's economic and financial situation during the war are, therefore, of considerable consequence for the international economic position of all European countries. Will Great Britain continue to buy large amounts of European goods? Furthermore, will Europe continue to have a surplus in the balance of trade with Great Britain?

“When Hitler has been defeated, the United Kingdom will, it appears, be found to have spent enormously of its economic world power.”⁴ Britain has drawn heavily on her foreign financial resources and has experienced a substantial increase in her external liabilities. These developments will have implications on her future international financial position. Since 1860 Great Britain has had a constantly increasing import surplus which was met from other income items in her balance of payments. On the average of the years 1936–1938 the British balance of payments was as follows (in £ million):

⁴ National Planning Association, *Britain's Trade in the Postwar World* (Washington, D.C., 1941), p. 5.

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<i>Debit</i>		<i>Credit</i>	
Imports	930	Exports	540
Government payments	10	Investment income	200
	—	Shipping earnings	110
Total	940	Commissions on banking, insurance, etc.	40
		Other receipts	10
		Total	900
Deficit			40

During these years Britain paid roughly 59 per cent of its import with exports, 26 per cent with investment income or liquidation, 11 per cent with shipping income, and 4 per cent with banking and insurance receipts.⁵ As a result of the war, income from the invisible items is threatened with serious reduction. Great Britain, which for one year fought alone against superior forces, used her economic resources at home and abroad just for one purpose—the prosecution of war. With her economy fully converted to war purposes she was unable to cultivate export trade and to supply her traditional markets with goods. At the same time she was obliged to import what she needed up to the limit of available shipping space.⁶ The quantity of exports

⁵ E. F. Schumacher arrives at the conclusion that the contribution of exports to the supply of the home economy with foreign materials amounted to only about 43.5 per cent. For the purpose of this account he deducts £176 million from both imports and exports since this amount represents the value of imported materials, which left the country again in the form of manufactured exports. See his *Export Policy and Full Employment* (London, 1943), p. 7.

⁶ In 1943 the total imports stood at £1,874.7 million (excluding munitions, at £1,216.8 million); at 1935 prices the total imports equaled 118 per cent of 1938 imports (excluding munitions, 79 per cent). The value of exports fell from £471 million to £232 million in 1943. British White Paper, *Statistics Relating to the War Effort of the United Kingdom*. (London, 1944), pp. 23, 45.

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in 1943 was reduced to only 29 per cent of the 1938 level. Of course, she did not have enough gold and foreign exchange to pay for her imports while her export declined so considerably. After spending about £650 million of her prewar holdings of gold and foreign exchange—about £500 million of it in the United States—she had to liquidate or pledge her securities and investments abroad. This process started in 1940 and is still going on.

At the beginning of the war British foreign assets were estimated at about £4,200 million, earning assets after the deduction of gold and dollar balances being worth £3,550 million.⁷ Though we do not possess any detailed figures as to how much of these assets were sold or pledged, various sources throw some light on the subject. In his budget speech on April 25, 1944, the Chancellor of the Exchequer stated that Great Britain had already parted with overseas assets to the extent of £1,000 million. According to the White Paper, *Statistics Relating to the War Effort*⁸ overseas assets to the value of £1,065 million had been sold up to June, 1944. Great Britain's liquidation of foreign investments was distributed as follows (in £ million): United States, 175; Canada, 186; South Africa, 125; Argentina, 25; India, 332. Furthermore, British securities worth £125 million are pledged in the United States against a Reconstruction Finance

⁷ About £2,250 million were in investments in the Empire; investments outside the Empire and the United States amounted to a nominal value of about £1,600 million, the real value being estimated at about half of that. Investments in the United States were £475 million. National Planning Association, *Britain's Trade in the Postwar World*, p. 7. Lord Kindersley estimated the nominal value of long-term overseas investments as £3,725 million in 1938 (*Economic Journal*, 1939, p. 643.) N. Kaldor put their market value at £5,000 million (*Economic Journal*, 1943, p. 261.)

⁸ P. 40.

Corporation loan of \$425 million. (By July 31, 1944 about \$125 million of this loan had been repaid.)⁹

The process of selling foreign investments is still going on, several countries continuing to repatriate securities held by the British.¹⁰ Great Britain has not only used a substantial part of foreign assets to pay for the supplies from abroad; she has, at the same time, incurred undischarged liabilities which at the end of 1944 are expected to reach the amount of £3 billion (\$12 billion; it surpassed \$10 billion in June, 1944). This amount represents blocked balances (credited to various parts of the Empire and to some other countries) which are usually called "Abnormal Sterling or War Balances."¹¹ Foreign-owned sterling balances at the beginning of the war totaled about £350 million.

During the current financial year, however, abnormal sterling balances are now piling up at the rate of about £1,000 million a year; this is explained by the virtual exhaustion of realizable overseas assets and by the increasing scale of war expenditure in the Far East.¹²

Even if we completely disregard the huge amounts which Great Britain has received from the United States through

⁹ "Sterling Balances and Britain's External Debt," *Foreign Commerce Weekly*, Oct. 28, 1944, p. 40.

¹⁰ South Africa repaid a debt of 180 million sterling and repatriated mining and other shares. *Economist*, July 31, 1943, p. 146.

¹¹ According to the *Economist* of May 20, 1944, p. 688, India had (in million £) 721, in April, 1944; Canada, 157; Eire, 133 (Dec., 1943); Australia, 74 (Jan., 1944); Egypt, 95 (Dec., 1943); Argentina, 42 (Dec., 1943); New Zealand, 31 (Nov., 1943); South Africa, 14 (April, 1944); Malaya, 58 (July, 1941).

¹² *Economist*, July 15, 1944, p. 89. "Every liquid investment has been sold," states Geoffrey Crowther in "British Twentieth Century Economics," *Yale Review*, Winter, 1945, p. 210.

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Lend-Lease, we realize the profound change in her position as a creditor nation. Particularly in computing postwar income from foreign investment, allowance must be made for the probable damage to the Malayan rubber plantations, to the mining facilities in Burma and Malaya, and the losses in Europe and elsewhere. Before the war Great Britain was the greatest creditor nation of the world. According to the perhaps too pessimistic opinion of some observers she may emerge from the war as a debtor nation, especially if we take into account the need to replenish her exhausted supplies.¹³ It is a sobering thought that Britain's net investment income may be about 60 per cent less than in the three prewar years, or about £85 million against £200 million in 1936-1938.¹⁴

Income from shipping is equally uncertain. At the end of June, 1939, the United Kingdom owned 28 per cent (or more than 15 million tons) of the world's ocean-going vessels as against the 16 per cent (8.4 million tons) owned by the United States.¹⁵ The losses in her merchant marine from submarine and air warfare reduced the total tonnage by 29 per cent at the end of 1943, and that in spite of the sizable production of the British and Canadian shipyards and of the purchase and temporary acquisition of ships from the United States and others.

¹³ Dept. of Commerce, *Some Factors in Post-War Export Trade with the British Empire* (Washington, D.C., 1944), p. 19.

¹⁴ "Sterling Balances and Britain's External Debt," *Foreign Commerce Weekly*, Nov. 4, 1944, p. 8.

The Chancellor of the Exchequer declared in the House of Commons on June 28, 1944, that it would be safe to say that Britain retains more than half of her 1938 overseas investments, including those in the British Commonwealth.

¹⁵ According to the *Economist*, of July 24, 1943, p. 101: "In 1936 the sea-going tonnage sailing under the British flag represented 36.7 per cent of the world total and carried 40.2 per cent of the world sea-borne trade. The total of United Kingdom tonnage was then 15,084,000 gross tons, the Dominion's 1,934,000, the

The United States merchant marine has been enormously expanded, and the new Australian, Canadian, and even the Indian, merchant fleets have also greatly been increased. It is doubtful that in the first years after the war the British fleet will be large enough to earn the prewar income. As to the future, Britain will have to expect sharper competition. Much will depend on the policy of the United States. Prior to the war the United States shipped only about one fourth (25.1 per cent in 1937) of its trade in American-owned vessels; it has now been suggested that its merchant marine should comprise a modern fleet of 16 million gross tons, plus a reasonable reserve,¹⁶ and that these ships should carry a liberal percentage (about 50 per cent) of American foreign trade.¹⁷ Unless a great expansion of overseas trade occurs, it can hardly be expected under these circumstances that the British income from shipping will reach the prewar level.

The income from insurance, banking, and other services seems to be equally uncertain. This income resulted from London's traditional position as international financial center, a position weakened by the decline in Britain's financial status. Foreign exchange control was, obviously, fatal to merchant banking, which earned commissions by financing trade in sterling throughout the world; many expect New York to inherit a large part of this business. To the international insurance business, foreign exchange control is equally harmful. London may recover the reinsurance business—that is, the underwriting of insurance policies on the Continent of Europe—temporarily taken

Empire total was 17,018,000 gross tons. The British trade at that time was estimated at 38.1 per cent of the world sea-borne trade.

¹⁶ Admiral E. S. Land, "Shipping's New Day," *Foreign Commerce Weekly*, Sept. 2, 1944.

¹⁷ *Foreign Commerce Weekly*, May 8, 1943, p. 7.

over by German companies. On the whole, the amount of income from various sources in banking, trade, and insurance will largely depend on the extent to which London regains its position as an international, financial, and trade center. And this will certainly take time.

Expecting that the war will reduce very severely the invisible items on the credit side, *The Economist* estimates that even if no other elements entered the problem, there would still be a yearly gap (including the prewar deficit) of at least £200 million on the credit side. It is clear that "the Battle of the Balance," the problem of how to meet this gap in the British balance of payments will be of paramount significance. The great question is what the British foreign trade policy after the war will be, and what measures will be taken to reduce the import surplus. Undoubtedly, the British policy will have great repercussions on the European Continent.

There are definite signs that Great Britain will, for a number of years, maintain import control, until she can appraise at least approximately the future trend in world trade. Import control may at first reduce the importation of luxuries. Next comes the problem of the import of foodstuffs. Great Britain's agricultural production has been remarkably expanded and technically improved during the war. Fifty per cent more land is being plowed up (19.4 million acres in 1943, compared with 12.9 million acres in 1939), and two thirds of wartime food needs are now being produced as against one third before the war. Britain is today the most highly mechanized farming country in the world. Mechanization has increased 110 per cent since the war began: 2,000 combines were employed for the 1943 harvest, and the number of tractors has risen from 50,000 to 120,000. Production of wheat, barley, and potatoes has more than doubled; produc-

tion of oats increased 58 per cent, fruits, 55 per cent, sugar beets 37 per cent, and vegetables 34 per cent.¹⁸ Altogether, the proportion of domestically grown food in the total food supply has substantially increased and the imported fraction has been reduced. There are evidences of a marked determination in Britain not to repeat the policy by which, after the last war, agricultural production was sharply curtailed, but to maintain the technical agricultural gains already made in the present war.¹⁹

While a fully employed Britain would need more foodstuffs, there still remains the question of how the expanded agricultural production will affect the import of food. The changed structure of the national income, which has resulted from the war and tends toward a further leveling off, may also have some bearing on the import of high quality food. There are many indications of a decline in the import of food, which has been a very important export item of continental Europe, especially of the Scandinavian and Low Countries. Moreover, seen from the European standpoint, one must realize that the competition with the overseas suppliers will be even keener than before the war. When supplies from the Continent were cut off, Great Britain was obliged to turn to overseas sources, particularly for animal products. Canada, the United States, Argentina, Australia and also West Africa, have become the main suppliers.

¹⁸ The caloric content of the production derived from the land of the United Kingdom is officially set as 70 per cent higher in 1943 than in prewar years both in terms of calories and of protein. Percentage increases of acreage are stated to have been, comparing 1942 with the prewar period: 82.9 for wheat, 51.8 for oats, 78 for "cereals," 102 for potatoes, and 66 for vegetables. The number of sheep, pigs, and poultry has declined by 25, 57, and 26 per cent, respectively, but the number of cattle increased about 7.6 per cent. *Statistics Relating to the War Effort of the United Kingdom*, p. 16. See also the *Economist*, Oct. 14, 1944, p. 54.

¹⁹ See the British Information Service publication *Post-War Planning in Britain* (New York, 1944), pp. 37 ff.

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These countries, especially the members of the Commonwealth, will certainly try to maintain at least a substantial part of their wartime gain on the British market. Some of them had heavily expanded production of animal foodstuffs. It scarcely needs to be pointed out that this fact will confront the European producers with complicated adjustment problems.

This situation may also influence the broader issue, namely whether Great Britain will continue the policy of imperial preferences and the shift toward a greater share of her trade with the Commonwealth. The effect of this policy in the prewar period can be illustrated by the following figures: Britain's import from the Empire went up from 29.1 per cent of the total import in the average of the years 1929-1931 to nearly 40 per cent in the 1936-1938 average. This question will be settled in connection with the development of the British foreign trade and also with the trade policy generally prevailing after the war.

In England much greater emphasis is now being laid on the expansion of export than before the war; everybody agrees that she can equalize her balance of payments only if she succeeds in increasing substantially her commodity exports. Opinions vary as to how great the increase must be, but most of the estimates set it at 50 per cent. How can such an increase be achieved in the postwar markets? From the standpoint of technology Great Britain will be, in some respects, stronger than she was before the war. The productivity of labor has increased, new skills have been acquired, and many war plants can be at least partially converted to peacetime production. Both government and industry are devoting much attention to the task of increasing industrial efficiency and improving production techniques. They are aware of the necessary shift in the composition of exports; they insist that Britain is first and foremost a processing

and servicing country and that its comparative advantage lies in adding brains and skill to the raw products of the earth. It will be relatively easy to maintain markets in such goods as fine woollens, Sheffield cutlery, whiskey, and sports apparel. The experts plan expansion in chemicals, plastics, engines and engineering supplies, and in various precision machines. It may be possible to take over some of the German markets.

There is considerable discussion concerning Britain's future policy on foreign trade. Few believe that it will be possible to abandon import control, in view of the changed structure of the balance of trade and the new developments on the world market. Some even go so far as to favor bilateral trade arrangements by means of which Great Britain could use the strong bargaining power of a big importer. While the majority fully recognize the great importance of multilateral trade to Britain, even *The Economist* considers a return to the system risky. A multilateral system within the sterling area, only, is recommended as a first step before a system of universal multilateral trade could again be adopted. If the future of British exports seems uncertain because of the progressing industrialization of the world keener competition and of the difficulties in adjusting production and trade to all these changes, how much greater is the dilemma of the European industrial countries. They must meet the same problems and more—the altered status of Great Britain itself, and without the advantage of a large sterling area. Undoubtedly it is in the interest of world trade to see Great Britain adopt the system of multilateral trade as soon as possible. It is equally in the interest of the American Continent, and especially of the United States.

Great Britain has been the greatest single customer of the United States and has maintained a very large import surplus.

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Her trade strengthened the position of continental Europe and Latin America—both important purchasers of American goods. American foreign trade policy will certainly have a decisive influence on the British policy. However, the United States can be helpful in an even more direct way. By assisting Great Britain to consolidate her international financial position and by granting her assistance for the huge reconstruction job, this country could renew the feeling of greater security in Great Britain, especially with regard to her future balance of payments. This might well overcome the very cautious attitude that appears to prevail in official as well as unofficial British circles. Thus, by helping Great Britain to regain her important role in international trade, the United States would likewise help continental Europe, to which the trade and export surplus with Great Britain are and will be of the utmost importance.²⁰

²⁰ John H. Williams rightly considers the solution of England's special difficulties to be the central postwar problem, and says that \$12 billion accumulation of sterling war balances in London . . . is not dissimilar in nature or in magnitude from the Inter-Allied debt or the Reparations problem that bedeviled international relations during the interwar period. *Foreign Affairs* Oct., 1944, p. 56.

CHAPTER SIX

WORLD ECONOMIC DEVELOPMENT DURING THE SECOND WORLD WAR

THE WAR has wrought profound economic changes in nearly all countries. The interruption of the international trade channels and the growing demand for war supplies gave a powerful stimulus to production. The export from the European Continent was almost completely cut off. The war in the Far East eliminated supplies of various commodities which the United Nations sorely needed. Everywhere great efforts were made to step up production; manufacturing capacity, in general was substantially expanded. The greatest absolute and relative expansion occurred in the United States, but the whole Western Hemisphere advanced to a great potential strength.

It is not our task here to describe in detail the economic development of the world in this period, and in any case it is not yet possible to gather comprehensive or accurate statistics. We shall try, however, to sketch roughly the main trends in production expansion in order to appraise its probable effects on trade. This expansion embraces nearly all countries and includes a wide range of commodities.

In the Western Hemisphere *Canada* ranks next to the United States in production achievements. It can be said that she will emerge as an *industrial* nation with a strong agriculture, that she will become a *creditor* country. Although before the war she already had the largest foreign trade per head, her dependence on export has grown even greater. The following figures speak for themselves: It has been estimated that the national produc-

tion has doubled during the war and has reached about 15 per cent of that of the United States; in the average of 1943, the general index of production was 259 against 100 in 1939 (268 in March, 1944). During the same period the index of mining production went to 242, the index of manufactures from 100 to 282. Among the manufactures the figures for textiles rose to 142, of wood and paper from 100 to 120. The number of persons employed in manufacturing increased from 660,451 in 1937 to 1,152,095 in 1942. Canada's major contribution to the war effort of the United Nations was in the production of basic raw materials—nickel, aluminum, magnesium, copper, lead, asbestos, lumber. In 1943, for example, Canada supplied about 40 per cent of the aluminum requirements of the United Nations, 90 per cent of nickel, 20 per cent of lead and mercury, 10 per cent of zinc and copper, and 75 per cent of asbestos; furthermore, she produced mica, tungsten, molybdenum, titanium, cobalt and magnesium.¹ Steel production has doubled since the war started, with the annual output reaching 3 million tons in 1943. New rolling and finishing mill and plate mills have been added and the steel-foundry capacity increased. Many types of steel are being produced which, before the war, had to be imported. When the war is over, the hydroelectric capacity will be 20 per cent larger than before.

As fourth of the United Nations war-goods producers, Canada has supplied a great variety of matériel ranging from aircraft,

¹ See Monthly Commercial Letter of the Canadian Bank of Commerce, May, 1944. Here are the most remarkable increases in the production of several basic materials (from 1939 to 1943); arsenic, 1,741,917 to 5,523,000; lead, 388 million lb. to 444 million lb.; magnesium to 7,149,525 lb.; mercury from 436 lb. to 1,709,000 lb.; molybdenum concentrate from 2,240 to 813,268 lb.; titanium ore from 3,694 to 73,723 tons; tungsten concentrate from 8,825 to 1,353,000 lb.; zinc from 394 million to 608 million lb.; aluminum from 100,000 to 500,000 tons; refined nickel from 64,500 tons to 93,300 tons.

naval vessels, merchant ships, trucks, armed vehicles and guns to explosives, small arms, ammunition, and signal and communication equipment. In the process, many new products were developed, among them machine tools, aircraft (aircraft engines, however, have not been built and are being imported), nylon, optical glass, plastics, synthetic rubber, radio and communication equipment. Shipbuilding has undergone vast expansion. More automobiles are being turned out. Textile industries developed new methods and new materials and expect to operate after the war with greatly increased efficiency. Canada's export in 1944 reached the record level of \$3,440 million.

When one considers the actual expansion, diversification of production, and technical progress achieved in the field of industry, it is fair to speak of an industrial revolution in Canada. And one may expect these achievements to be surpassed in the future. At present rates of efficiency, workers actually employed will be able to produce a vastly larger volume of civilian goods than Canada has ever known. The industrialization of Canadian economy is reflected in the composition of national output, of which manufactures represent virtually one half. Capital invested in industries has increased nearly to 50 per cent.

There will, of course, be a difficult reconversion problem, since not less than 55 per cent of the industrial machinery is engaged in war production. But it has been stated that 90 per cent of the present capacity can be converted to peacetime production, a reconversion that will be made easier because the equipment of most of the factories is modern and in good condition. Naturally Canada is devoting considerable attention to postwar trade relations, and is expected to promote her export with a liberal foreign credit policy. However, the problem of readjustment will be of major proportions.

For the Continent of Europe and for Great Britain the development in the *Latin American* countries will be of great significance because of their considerable trade relations before the war. In 1938 total Latin American exports were valued at \$1,834 million, and total imports at \$1,488 million. Continental Europe took 35 per cent of the exports, Great Britain, 19 per cent, Europe altogether 54 per cent against 30.5 per cent purchased by the United States. Continental Europe supplied 35 per cent of the total import, Great Britain 12 per cent, Europe total 47 per cent, while the share of the United States was 34 per cent. Continental Europe's export to Latin America totaled in 1938 \$510 million (or about 14.5 per cent of Europe's export outside the Continent) ² and that of the United Kingdom \$187 million.

The war interrupted these established trade channels not only with continental Europe but also with Great Britain. The lack of shipping space and Britain's inability to export civilian goods because of her complete mobilization for war cut her share in Latin America's export to 12 per cent in 1943, and in import to only 7 per cent. During the war Latin American trade with the United States has greatly increased. This is especially true of exports, as the United States is purchasing all kinds of strategic materials from Latin America, in a largely successful effort to replace goods previously imported from other countries. In 1943 the total export of Latin America reached \$2,381 million, of which 56 per cent or \$1,310 million went to the United States. The value of imports remained on the prewar level, the share of the United States reaching \$721 million, or 55 per cent in 1943. It is unlikely that this great shift in the geographical

² In the same year continental Europe exported to the United States goods for \$450 million.

distribution of foreign trade will remain fixed after the war or that the prewar situation will be reestablished. Here, too, many adjustments and new developments are to be expected.

The economy of Latin America, and especially of the South American countries, has been influenced by the following facts: The blockade introduced immediately after the outbreak of the war and the disruption of trade relations with Europe caused growing difficulties in the import of manufactured goods and, to some extent, in the export of raw materials and foodstuffs. This development strengthened the trend toward industrialization in a number of countries. After entering the war, the United States could not satisfy the demand for industrial commodities which accompanied the improvement of the general economic situation of Latin America. This fact, together with rising prices, further stimulated industrial production in many countries, especially in Brazil, Argentina, Mexico, Chile, and Peru. The situation would have favored an even greater increase but industrialization was limited chiefly by difficulties in obtaining enough of the needed equipment and very soon, also, by a lack of skilled labor and technical personnel.

While, at first, the outbreak of the war hit the export of some raw materials, particularly metals, that were previously sold to the European Continent (23 per cent of the exported copper, about one third of lead, zinc, antimony, and manganese), later the situation changed entirely: in 1941 the United States developed an enormous defense program and was spurred to still greater effort after Pearl Harbor. Latin America (with the exception of Argentina) was, to all purposes, included in this program, and was assisted, technically and financially, in expanding the production of many strategic materials. After supplies from the Far East were cut off, the United Nations en-

deavored to obtain from Latin America various products previously imported from Far Eastern sources.³

The United States Government agencies concluded agreements with several American countries for the exclusive purchase of many strategic materials, including most of the metals.⁴ By virtue of these agreements the exporting countries obtained assurances of a market for fixed quantities of specific commodities for a definite period (usually five years). The result of this policy was a greatly enlarged production. Export to the United States, which in 1938 amounted to \$548 million, reached \$977 million in 1942 and \$1,310 million in 1943; the export surplus was \$294 million in 1942, \$599 million in 1943, and \$320 million in the first six months of 1944. By 1941 Latin-American production of nonagricultural raw materials had reached a high level (1938 = 100): metals, 119, nonmetallic minerals, 106; wood products, 136; fuel and power, 115.

The figures have continued to rise. Production of copper in Chile rose to 500,000 tons, and in Mexico to 50,000 tons; tin production in Bolivia went up to 43,000 tons from only 26,000 tons. Brazil increased the output of manganese to more than 200,000 tons and also furnishes chrome ore, tungsten, quartz, industrial diamonds, mica, and asbestos. Mexico, Argentina, Peru, and Bolivia deliver zinc and lead; Cuba, chrome ore; Mexico, mercury and graphite. Bolivia increased production of antimony ores from 10,000 to about 15,000 tons, while Mexican

³ Rubber, tin, tungsten, cinchona, fiber, mica, sisal, kapok, vegetable oils. See Foreign Economic Administration, *Report to Congress on Operations*, Sept., 1944, pp. 18 ff.

⁴ Copper, lead, manganese, tin, tungsten, zinc, then for rubber, wool, quartz crystals, and cinchona. For the fiscal years 1941–1943 the United States Government paid for the purchase of strategic materials and ships (including capital outlays to facilitate procurement) the amount of \$1,102.6 million. A. P. Whitaker, ed., *Inter-American Affairs, 1943* (New York, 1944), p. 219.

output of tungsten, Peruvian output of molybdenum, vanadium, and tungsten also rose. Thus, to a great extent, Latin-American sources replaced India, the Soviet Union, and the Gold Coast in supplying the United States with manganese ore, Spain and Italy in supplying mercury, China in supplying tungsten and antimony, Turkey and Africa in supplying chrome ore, and India in the supply of mica. The most important development in the production of minerals took place in Brazil, Chile, Peru, and Bolivia. Mexico's mining industry experienced a rejuvenation.

In food production the increase of rice, cocoa, and especially of vegetable fats and oils should be noticed. Before the outbreak of war in the Pacific, the Western Hemisphere imported yearly about 2.5 billion pounds of vegetable oil and oilseeds, primarily from the Far East.

The process of *industrialization*, which, during the last twenty years, has been going on almost everywhere in this area, has been speeded up by a further expansion of manufacturing industries, ranging from steel and iron to glass, leather, and plastics. To mention only a few outstanding examples: ⁵ In Brazil a new steel mill with an annual capacity of 350,000 tons will be able to meet a large part of the country's need for steel and basic steel products. Production of light steel rails is under way, and will shortly be followed by production of heavier rails. Thus,

⁵ The general index of industrial production in Chile increased on a yearly average from 158 in 1939 to 179 in 1943, in Mexico from 119 in 1939 to 133 in 1942. The number of industrial establishments in Brazil increased by some 15,000 since the outbreak of the war; the number of industrial workers went up from 825,000 to one million. In Argentina the wartime increase of manufacturing surpassed 20 per cent. The index of the volume of industrial production reached 155 in 1942 against 100 in 1935, and 133 in 1939 (the value indices for these years were: 100 in 1935, 145 in 1939, and 210 in 1942.) In May, 1943, the employment index had risen to 125 against 111 in 1940. The gross value of industrial production exceeded that of agricultural production in 1935 by 14 per cent, and in 1943 by 132 per cent.

for the first time, rails will have been produced in South America. Mexico, which in 1941 produced 164,800 tons of iron and steel, expanded its steel plants and is erecting a new one. Plans have been advanced to increase production in Chile to 50,000 tons a year. In Argentina steel pipes are being manufactured, using sheets produced by the Military Steel Works. A new plant with an initial output of 25,000 to 30,000 tons is being prepared in Colombia. A small rolling mill has been erected in Uruguay. In 1942 the Peruvian government signed a contract with United States contractors for the exploitation of iron and coal deposits, the installation of a blast furnace, and steel-producing and finishing mills. A similar impetus is reflected in the chemical industries. Soda and caustic soda are being produced in Brazil, Argentina, Colombia, and the production of chlorine has been increased. Chiefly as a result of the cessation of imports from Germany, chemical and pharmaceutical industries (and plastics) in Chile, Mexico, Argentina, Peru, Colombia, and Brazil have been expanded. Brazil will have a paper mill with a capacity to produce 40,000 tons of newsprint, and 40,000 of pulp, and in Mexico and Argentina the paper industry has been enlarged.

The development of textiles was enormously spurred by the scarcity of goods, which were obtainable from abroad only with great difficulty and in very limited quantities. Brazil and Mexico have both become large exporters of cotton cloth. To make the best use of the available equipment, many factories work on a twenty-four hour basis. The wool industry has taken great strides in Uruguay, Argentina, Peru, Chile, and Brazil. Tire factories were erected in Argentina, Brazil, Peru, Cuba, and Uruguay. Production of rayon on a small scale was begun in Mexico, Argentina, Chile. The leather industry has made sig-

nificant progress. Flat-glass manufacture was started in Brazil, and plants are being prepared for Chile and Argentina. In a number of countries cement production has grown considerably.

In addition to those already mentioned, the list of new industries started in Brazil includes complicated manufactures as electrical appliances, including radio equipment, certain types of machinery, and even ships. As to Argentina there has been an increase in smelting of nonferrous metals, in the production of agricultural machinery, of edible oils, paper and cardboard making, production of china, crockery, and glass, food processing, clothing, washing machines, rayon, radios, electric bulbs, and railroad cars.⁶ There has even been a tendency to develop various industries for export, which reached in 1943 the amount of 424 million pesos, or 19 per cent of the total, against 45 million or 3 per cent of total exports in 1939; the chief items here are textiles, leather manufactures, and chemical and pharmaceutical products.⁷

Great efforts are being made to improve the fuel situation. In several countries new installations of hydroelectric power have been made; projects are already under way in Brazil, Chile,

⁶ See Whitaker, *Inter-American Affairs*, 1943, pp. 108 ff.; Foreign Policy Reports, May 1, 1944; *Economist*, July 31, 1943, p. 143; *Foreign Commerce Weekly*, Aug. 28, 1943; Annual Reports of the Banco Central de la Republica Argentina. Felix J. Weil, *Argentine Riddle* (New York, 1944); S. E. Harris, *Economic Problems of Latin America* (New York, 1945), Chapters I, II. This book was published while the present study was in press.

⁷ The following index numbers of employment indicate the increase in manufacturing production in Argentina (1937 = 100):

	1939	1942	May, 1943
Textiles	107.2	129.2	136.7
Leather and leather products	116.6	127.7	130.1
Chemical and pharmaceutical industry	119.5	127.3	139.9
Paper and paper products	109.3	134.7	138.2

Colombia, and Mexico, and in other countries they are in preparation.

Under the impetus of the war, manufacturing progress would have reached even greater proportions, if sufficient machinery, technical personnel, and skilled labor had been available, and, finally, had it not been for the shortage of fuel and electric power. Transport difficulties also presented an obstacle. On the other hand within the limits set by her own war needs, the United States has assisted in the industrialization of the Latin-American countries in order to increase their production of strategic materials and to help raise their purchasing power as a basis for an expanding foreign trade.

A great surplus of the balance of trade has resulted from the substantially increased export to the United States and has profoundly improved the position of Latin America with regard to her holding of gold and foreign exchange. Revealed Latin American gold and foreign exchange holdings, chiefly in dollars, increased from \$900 million in 1939 to some \$3,500 million by the middle of 1944.⁸ In addition, several countries have repatriated securities owned in Great Britain and in the United States, thus reducing their foreign indebtedness.

Production and productive capacity of minerals and manufactured goods (chiefly consumer goods) throughout Latin America has been enlarged extensively during the second World War; the increase of industrial production is estimated at least at 20 per cent. The export to the United States has more than doubled, the total export rising by about 40 per cent. The position of the balance of payments has greatly improved. The obvious question rises as to how this new and expanded production will be maintained a few years after the war. Who will buy all

⁸ Bulletin of the National City Bank, Aug., 1944, p. 93.

these quantities of metals and minerals, some of which apparently were not produced at low cost? How can the new manufacturing industry compete with the old prewar concerns in Great Britain and continental Europe, whose goods will have to be purchased if the Latin Americas want to continue to export many primary products in return? The producers of these commodities will certainly press toward regaining their old outlets.

Nevertheless, the memory of the crisis in the thirties is still fresh; and the Latin American countries do not want to depend on the export of a small number of primary products. They are trying to attain a more diversified agriculture and a better balanced economy, and progressive industrialization is definitely an accepted objective in most of these countries. Nine of them (Argentina, Bolivia, Colombia, Chile, Ecuador, Haiti, Mexico, Peru, and El Salvador) have enacted legislation providing for the establishment of industry-promoting institutions,⁹ and the eleven remaining governments have introduced various measures to promote economic progress. Development corporations and financing institutions have been created by the governments, which in several cases have directly entered into business. Furthermore, it is expected that the lack of capital will be overcome by the direct participation of business firms of the United States in various important enterprises.

Whatever the eventual policy will be, it will have to cope with some difficult adjustment problems. Though industry will not be confronted with the task of reconversion from war to peace production and will enjoy the advantage of producing chiefly for the domestic market, it will be hard to find world markets

⁹ Whitaker, *Inter-American Affairs*, 1943, p. 124; L. L. Lorwin, *Postwar Plans of the United Nations* (New York, 1943), pp. 152 ff.; S. E. Harris, *Economic Problems of Latin America*, pp. 29 ff.

commensurate with the productive resources of Latin America and other surplus regions of the world, even if we assume economic activity in the world at large on a higher level than that which prevailed before the second World War. There is no doubt that Latin America will enter the postwar period financially as well as economically stronger than she was before the war.

Throughout the *British Commonwealth*—particularly after the defeat of France—production was mobilized to help the common war effort. In parts of the Empire further expansion was hampered by the lack of skilled labor, tools, machinery, and transport facilities. Second only to Canada in production increase, India has become the eighth industrial country in the world. Production of iron and steel has increased by 40 per cent; considerable strides have been made in producing special steels and a ferroalloy industry has been started. Production of aluminum has begun, high explosives are now being made, and large chemical plants have been installed.¹⁰ New works for making alloy steel have been brought into production, and all kinds of ordnance, arms, and ammunition are being manufactured on a large scale. The production of armored vehicles and armored cars, of certain classes of machinery and machine tools has also been undertaken, while Indian shipyards, vastly expanded, are being used for the construction of minesweepers, patrol boats, motor launches, and other small vessels. Considerable progress has been made in the production of electrical items and cables. India manufactures complete bodies for imported car chassis. The output of textiles has grown from 118 in 1939 to 175 in

¹⁰ For the manufacture of nitric acid, synthetic ammonia, caustic soda, glycerin, and sulphuric acid, and, further, for the production of crude benzol and toluol on a big scale.

1943. Leather manufacturing has increased and in the tanning industry good progress has been achieved; India has become an important supplier of army boots. The timber production has doubled, manufacturing of paper has grown by more than one third. This wide-scale industrial activity further includes brushware, woodware industries, crockery, cutlery, cardboard products, plywood, glass and glassware, medical instruments and pharmaceutical products; and such domestic items as cement, matches, soap, and paint. The expansion would have been even greater, except for coal and transport shortages. The British helped to provide skilled labor by establishing special training centers and by sending many workers to Great Britain for further training.

The pattern is repeated in Australia. Here the index of the number of workers employed in manufacture went up from 100 in 1939 to 135 in 1943. During the first three years of the war the number of factory workers increased from 565,000 to 725,342 in 1942, and during the same period the value of output rose from £500 million to £773 million. (The value of fixed capital went up to £75 million, or more than 25 per cent.) "In manufacturing the war pushed Australia ahead, perhaps 20 years."¹¹ Many factories were built to equip the Australian and other armies and to satisfy civilian needs. The steel industry has increased production by 45 per cent to 2,200,000 tons annually and now produces many types of steel which were previously imported. Australia produces her own metals for armor plate, steel cables, bearings, motor and airplane parts and bodies, guns, small arms, precision instruments, and wireless sets. All types of machine tools are being made, as are most of the 150 main chemicals

¹¹ Mr. Spender, a member of the Australian Advisory War Council, in the *New York World Telegram*, Feb. 11, 1945.

needed for explosives.¹² The optical-lens industry is an important wartime development; a fine quality glass is being manufactured. The first newsprint mill has been put into operation. Production of locomotives on a small scale has been started, and the food processing trades have been greatly expanded. Several new mills for cotton textiles were established, and the manufacture of woolen cloth rose. Agricultural production has been reorganized so that war requirements can be met more adequately. It can be assumed that after the war Australia will be a more highly industrialized country than she was before, and that this development will change the structure of its foreign trade, especially its imports.

Even agricultural New Zealand has evidenced the general trend. There is a new asbestos plant and larger quantities of woolen goods, footwear, biscuits, and wood products are being made. In 1942 the following items were produced for the first time or were further developed: metal buttons, inks, typewriter ribbons, potato-sorting machines, gas producers, leather bags, and enamel products. Important progress also occurred in the new linen-flax industry (by 1943 a total of 23,000 acres of flax was under cultivation, 17 factories were processing flax).

South Africa's development in the war period would in normal times have taken twenty-five years.¹³ Industrial workers reached in 1943 the index of 160 as against 148 in 1939. In the iron, steel, and engineering industry a great expansion took place. This was

¹² Dept. of Commerce, *Some Factors in Post-War Export Trade with the British Empire* (Washington, D.C., 1944), p. 35. See also Wilson C. Flake, "Australia: the Dramatic Course of Its Wartime Economy," *Foreign Commerce Weekly*, Dec. 9, 1944.

¹³ South African Public Relations and Information Service, *South Africa at War* (Washington, D.C., 1943). This source indicates the total of 741,576 workers in 1943 as against 352,000 in 1938-39.

made possible by the existence of the heavy engineering industries serving the needs of the great gold mines.

New steel plants were brought into production to increase the prewar output of 325,000 tons to 600,000 tons yearly. A plate mill is being constructed with a range capable of supplying practically the whole of the Union's own requirements. The output of farm machinery has been more than doubled, and the food industry has been spurred. South Africa has done a great job in assembling and equipping armored cars and other vehicles for the army (the engines had to be imported). A machine tool industry has been started. Quantities of shoes, blankets, and garments were made for the armed forces and radio parts were manufactured. In munitions South Africa made at least a tenth as much as Great Britain, and in some cases the output was up to 45 per cent. There has been extensive manufacture of overhead traveling cranes, and the construction of engineering equipment and of electric installations has greatly advanced. Great quantities of tin, enamelware and other equipment for use in field hospitals and kitchens were made. Altogether, 364 new products were made in 1942 alone, chiefly in the steel, metal, chemical, machinery, electrical, leather, tanning material, and plastic industries. Woolen goods, cotton manufactures, and fertilizers, all previously imported, are now being made at home.

Among the increased supplies from the British colonies we may mention copper and tungsten from Rhodesia, tin from Nigeria, bauxite from British Guiana, chromite from Sierra Leona, manganese from the Gold Coast. Flax factories are being erected in Kenya, power alcohol and diesel fuel are being made in Uganda. Under the stimulus of war needs, secondary industries, mostly on a small scale, are being developed in a number of colonies.

In the Belgian Congo the mineral output has increased. The production of copper ore surpassed 200,000 tons yearly, nearly doubling the prewar output, and production of tin, zinc, and lead ores has been expanded. Rarer metals, as uranium, tantalite, radium, and industrial diamonds, which are important in a world at war, are now extracted in substantial quantities. Increased production of palm oil and copal should also be mentioned.

Throughout the *Middle East*, particularly in Palestine, remarkable progress in industrial expansion has likewise been achieved. The number of workers employed in industry has been doubled. The principal industries are clothing, leather, metals, chemical and pharmaceutical products, and diamond cutting. A superphosphate factory near Tel-Aviv works up the Trans-Jordan deposits of phosphate rock. In Syria and Eritrea lignite mining has been developed. Iran supplies millions of pairs of army boots to Russia. To increase food production the Middle East supply center has arranged for the importation of agricultural machinery; the area under cereal crops has grown by more than two million acres.

Yet the expansion of production in the *United States* overshadows all similar developments elsewhere. However, as the gigantic achievements of this country in all fields of economic life are well known, we can limit ourselves to mentioning only a few facts. While an army of eleven million men was being created, national production swelled at the same time to enormous dimensions. Thus the United States has become the only country able to satisfy both military and civilian demands—in other words, to have both guns and butter. According to the Index of the Federal Reserve Bulletin, in 1943 industrial production reached 239 (physical volume) compared to 109 in 1939; production of durable manufactures, 360 (109 in 1939),

nondurable, 176 (109 in 1939); and production of minerals, 132 (106 in 1939, and 143 in October, 1944).¹⁴

The total productive capacity of the United States has been increased by almost 50 per cent during the war¹⁵ and now amounts to about 45 per cent of the capacity of the world. The production of light metals and ferroalloys, of fighting planes and other aircraft, merchant ships and war vessels, tools, and capital goods, in general, has been enormously increased. Enough synthetic rubber is made to meet the total peacetime demand for rubber. Manufacturing of all kinds of plastics has made large strides. Great deeds were achieved in the technological progress of nearly all branches of industry. Production of various minerals was expanded, new mines were opened. Production of food in 1944 reached a level 33 per cent above the 1935–1939 prewar average. Lend-lease supplies, reaching \$36.5 billion by January, 1945, have brought the export figures to a record height of around \$14 billion yearly; but even import figures have gone up, reaching \$3,377 million in 1943 against \$2,318 in 1939. With this enormously expanded productive capacity the United States will emerge from the present war as the biggest industrial power and strongest financial factor in the world.

We do not now possess detailed statistics concerning this universal expansion in productive capacity, because a great part of

¹⁴ In the group of durable goods the index figures (adjusted for seasonal variations of production) for October, 1944, are: (1935–1939 average = 100) iron and steel 206, machinery 429, transportation equipment 706, nonferrous metals and products 236. In the group of nondurable goods: textiles and products 147 (rayon 198), manufactured food products 148, paper and paper products 142, petroleum and coal products 265, chemical products 306.

¹⁵ National Planning Association, *America's New Opportunities in World Trade* (Washington, D.C., 1944), p. 49.

the information is withheld for military reasons. It is, nevertheless, possible to see clearly the trend of the whole development outside Europe. There have been two large areas of industrialization—one in the countries of Latin America, and the other in the nations of the British Commonwealth. The increase in the United States represents another most important factor in the over-all situation.

Some estimates place the wartime increase of world production (not including the United States) at 20 to 25 per cent. War needs have led to the expansion of production of raw materials, particularly of minerals. Production capacity for capital goods has had a greater increase in the industrialized countries, whereas production of consumer manufactures was expanded in many agricultural countries. It has become an established policy of a large number of agricultural countries to continue industrial development even after the war. While the international financial position and the balance of payments of Great Britain and the European Continent has deteriorated, the corresponding position in other countries has improved. There the situation is characterized by the increase of gold and dollar holdings, by blocked sterling balances, and by the repatriation of public debts and other securities held abroad.

There is certainly no doubt that nearly all overseas countries will face problems of postwar production adjustment which will, obviously, be of different intensity and magnitude. However, contrary to the countries of continental Europe and in many respects also to Great Britain, they will not be confronted with the tasks of relief, rehabilitation, and reconstruction, and they will enter the postwar period possessing substantial reserves and with their national economies on the whole strengthened. They will, furthermore, enjoy one very important advantage as com-

pared with nations lately under German rule: they will have preserved the continuity of political life and social structure; they will not have been shut off from the rest of the world; they will have continued to participate in international trade, and they will have been able to plan for postwar reconversion and changes. For all these reasons their position will be relatively easier than that of Europe and will make possible the speedy initiation of postwar work.

CHAPTER SEVEN

INDUSTRIALIZATION AND EUROPE'S TRADE

HOW WILL expansion in other continents affect the European export markets? Immediately after the war, when the demand for goods will be great and the supply short, it will hardly be a problem to sell European commodities. But we must look at the question from a long-range view. A good many countries are now supplying the market with items once bought from Europe. How will this new industry compete with the older, more experienced one, whose products are better known? To provide an even approximately satisfying answer it would be necessary to examine each industry separately, taking country by country. At this moment this is not possible; it is even difficult to guess the probable conditions of production in Europe after the war.

The industries concerned will certainly themselves undertake such studies. In many fields the new overseas competition will be technically efficient and, with further improvement will be able to compete. This may be the case in a great part of the textile industry,¹ in some parts of the chemical and metallurgi-

¹ The following figures (*Economist*, 1944, p. 150) from the Report on the Post-war Problems of the Cotton Industry prepared by the Board of Trade in London indicate the development of the cotton industry in some countries up to 1942 (in million square yards):

Country	Production		Export	
	1937	1942	1937	1942
United Kingdom	3,806	1,850	1,921	485
United States	9,321	12,000	236	410
India	5,548	5,800	377	940
Brazil	900	1,400	7	250
Canada	345	350	5	20

cal industry, in the leather and shoe industry, the small engineering trade, and others. On the other hand, some industries and factories built to relieve shortages during the war have been considered uneconomical from the very beginning, and cannot be expected to survive normal postwar competition (for instance, rayon factories with 300 tons yearly production). Obviously, any adjustment to the world market can be brought about only by competition operating within a system of freer trade. It is probable, however, that since new vested interests have been created everywhere many countries will grant protection to a great number of the new manufactures that supply primarily domestic needs. European exporters must count on these changes in their market, first of all in countries where a new national industry has been established and enlarged.

Competition on the overseas markets will stiffen. The United States will try to find new markets abroad; Great Britain will be compelled to increase her export; Canada is looking to Latin American markets; and some of the industries in Latin America (for instance in Brazil and Argentina) will try to maintain a part of the markets newly acquired during the war. Australia hopes to supply some of the markets in the South Pacific and in Southeast Asia, and even the Union of South Africa is preparing to sell goods in Central Africa.

Much will also depend on where American industry buys its

The production of woollen and wooled tissues declined in Great Britain from 90.5 million lbs. in 1938 to 44.2 million lbs. in 1943; in the U.S.A. the mill consumption of apparel wool was doubled from 1939 to 1943, in Canada from 1938 to 1939. Great increase took place in the four great wool producing countries, Argentina, Australia, New Zealand and Uruguay. (*Economist*, 1944, p. 791.) While during the war the British export of textiles has greatly declined, the export from the continental textile producers to the outside of Europe has practically ceased; and it represented an important item for some countries as Czechoslovakia, Italy, France, Switzerland, Germany, and Belgium.

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great amounts of raw materials. Consider what the loss of the American market for rubber would mean to the Malayan States and the Dutch East Indies—and indirectly to the European countries exporting to these areas. This applies also to various other products. If the United States continues after the war to buy strategic materials from Latin America, thus supplanting other prewar sources, her export to Latin America will doubtless increase while Europe's declines—not only to Latin America but also to the countries which lost some of their markets in the United States.

Thus, we could go on to demonstrate the profound changes in world trade resulting from the present war. In every respect they have been more intensive than those of the first World War. The greater requirements of the war economy brought forth a greater expansion and conversion of production. The war is lasting longer and has spread farther; its guns are heard literally around the whole world. During the first World War the European countries were able to maintain a certain commercial contact with the rest of the world. This time, with the exception of the small trade of the few neutral countries, the Continent has been completely cut off. For all these reasons the impetus for industrialization has been stronger. The changes initiated by all these developments will be more extensive; the task of readjustment, of creating new equilibrium, in the world economy will be more complicated.

Although the repercussions of the first World War on world production and international trade were less drastic, readjustment was hard and slow; indeed, in the whole interwar period no real equilibrium in world economy has been achieved. This failure should serve as a warning and a lesson to us now. In general we are giving more attention to the problem of primary

production than to manufacturing and are planning to check any abrupt decrease in prices of primary products that may result from a sudden drop in wartime demand. It has been suggested that such a fall in prices should be prevented by concluding commodity agreements and by accumulating strategic stocks (having the role of buffer stocks) of some of these products. It is rightly argued that success in this field would also help in maintaining markets for industrial goods.

The expansion of industrial production during the war has not followed any preconceived plan. It was stimulated and dominated by two factors: direct war requirements and the shortage of goods resulting from reduced imports. The decision as to what plants would be built or expanded depended on the availability of machinery, skilled labor, and technical assistance. Once normal conditions return, the respective governments and the owners of the new industries will make every attempt to correct whatever weaknesses are found in them. Moreover, the tendency will prevail to supplement the industrial structure within the domestic economy. The war has stimulated the existing policy of industrialization, which will not end with the end of the war. To industrialize agricultural and backward countries has become a part of the present economic program, which is designed to lead to a general development of the world economy and to an increase of the standard of living all over the world. Even countries with advanced agriculture look to secondary industries as a needed supplement to their economic structure, especially if there is a resumption of the unfavorable prewar trend in trade terms between agricultural and industrial products. The process of developing the production of retarded regions will be pushed ahead, whatever may be the attitude of the countries now holding industrial leadership. As the situation

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comes into clearer recognition, the industrialization of backward countries is becoming the subject of international discussion.

One must realize that technical knowledge has increased throughout the world; new skill has been acquired and the countries have learned that it is possible to build industries quickly. The Russian achievement in this particular field—the fact that the Soviet Union was capable of creating big industries of capital goods without extensive foreign technical help—serves as encouragement to the postwar plans of other nations.

As we have seen, the leading Latin-American countries are determined to go ahead with their industrialization programs; they will not hesitate to protect, as they have done in the past, all industries considered important and technically sound.² This is indicated by the fact that most of the respective governments have already actively sponsored industry-promoting institutions and in many cases have taken over further industrial development as a foremost task of government itself. Their endeavor is strengthened by the expectation that the United States will assist them and cooperate with them in developing their domestic resources, and the gold and dollar balances accumulated during the war will enable them to import the needed equipment. As far as can be judged now, the American government and business world both consider the economic development of Latin America, obviously comprising industrialization, an appropriate path to mutual expansion of trade.

The enormously increased production capacity of capital goods in the United States is one more reason for this country's

² See Samuel Guy Inman, "Some Latin American Views on Post-War Reconstruction," *Foreign Policy Reports*, March 15, 1944. See also Whitaker, *Inter-American Affairs*, 1943, pp. 124 ff.

interest in the advancement of the agricultural and backward countries in general. China also wants to start a huge development program after the war. "The present war has made us [the Chinese] realize that industrialization is indispensable if we are going to raise the living standards of our people and increase the strength of our nation."³ A detailed program is being prepared to specify what industries could be built and within what time. While the Chinese expect that a number of the future industries will undoubtedly be capable of existing without the artificial support of tariffs, they anticipate that the "light" industries (textiles, leather and matches, chiefly the fields in which, before the war, the Japanese had been formidable competitors), will be in urgent need of protection.

In India very ambitious schemes for industrialization are being prepared. The most far-reaching among them is the so-called "Bombay Plan," a document prepared by the Bombay industrialists as a "Plan of Economic Development." The objective is to double the national income per head within fifteen years after the plan is put in action. Some detailed aims are stated in clear terms.⁴ Priority is given to these basic industries: electric power, mining and metallurgy, machinery and machine tools, chemicals, transport, cement, and armament. The Indian Federation of Labor has produced a similar "People's Plan." Although many doubts are raised as to the possibility of realizing these very ambitious schemes, it can be taken for granted that the increasing political strength of India together with the eco-

³ "International Economic Development," by Dr. Ching Chao-wu, in "What the Chinese Think about Post-War Reconstruction," *Foreign Policy Reports*, Nov. 1, 1943. See also Lawrence K. Rosinger, "China as a Post-War Market," *Foreign Policy Reports*, Jan. 1, 1945.

⁴ See the *Economist*, June 17, 1944, p. 804; also G. D. Birla, "Industrialization in India," *The Annals*, May, 1944, p. 120.

economic effects of the war will be a powerful stimulus for further economic, and especially industrial, development. India's balances in London, which have already reached \$4 billion (more than half of the prewar national income) will in the first place be used to import capital goods needed for economic development. The British government will not, and probably cannot, object to this use of India's balances; British industry may welcome it as providing markets of a promising duration for capital goods.

The future of the existing industries and their improvement is foremost in the minds of the Australian government. In the Union of South Africa the "Industrial Development Corporation" was set up by the government in 1940 with the purpose of guiding the promotion of new industries and rendering a measure of financial assistance.

During the years immediately preceding the war the agricultural countries in Eastern and Southeastern Europe were undertaking considerable expansion of industries; they consider further industrialization necessary for their economic progress in general and for the relief of their agricultural overpopulation in particular.

The Soviet Union will certainly make every effort to rebuild what was destroyed during the war. She will continue to promote industrial production in those territories to which, during the war, some industries were moved from the areas temporarily occupied or threatened, and she will attempt to develop new industries. In spite of the war Russia has achieved remarkable success in the maintenance of industrial production. Judging from the past, it is fair to assume that ambitious plans for future industrialization of the country will be worked out and put into operation. The economic development in the victorious Soviet

Union will certainly embrace more diversified industries; like some other nations, Russia, too, expects the United States to cooperate in this task, especially by supplying tools and machinery.⁵

The impetus for a rapid expansion of production throughout the world, especially in the field of manufacturing, which results from the second World War, overshadows greatly the effects of the last war. We can speak of a new industrial revolution. It can be assumed as certain that this development must change the structure of world trade.

Enlarged industrial production in agricultural countries will undoubtedly replace many of the imported goods. It will change the import structure of countries newly industrialized, as well as those industrially advanced. During the period of new industrialization the import of capital goods will increase, and there will be a continuous demand for spare parts and for machinery for replacement and improvement. Import of semi-manufactured goods may rise. Assuming that industrialization increases the wealth of the nations concerned, we can anticipate a greater demand for goods previously imported in small quantities, and on the whole a greater demand for goods of higher quality.⁶ The intensity of these expected shifts in imports will obviously depend on the economic structure of the countries where the new industries are established. Thus the introduction

⁵ The Russian demand for American capital may approximate one billion dollars yearly for ten or fifteen years after the war. National Planning Association, *America's New Opportunities in World Trade*, p. 54.

⁶ As H. Frankel rightly remarks, industrial planning should be linked with social planning, creating a larger market for foreign goods. If the bulk of the population does not benefit, from the increase in national income associated with industrialization, the industrialization holds some dangers in the old industrial countries. "Industrialization of Agricultural Countries," *Economic Journal* (London, 1943), p. 188.

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of new industries, for instance, in the United States or in Canada, replacing these products previously imported, will hardly lead to an increase in the import of other products and might result in a reduction of trade. Industrialization of poorer and overpopulated countries will probably have an *expansionary* effect on world trade, if and when a general increase in the standard of living occurs. On the other hand, industrialization of agricultural countries with a specialized primary production and a relatively high level of living, and which also possess the raw materials needed for manufacturing, might not have the same effect of creating vast demands for new goods. The already existing demand, formerly met by imported goods, will now be satisfied with domestic manufactures.

Larger industrial production will lead to a greater demand for raw materials in so far as the demand of the newly industrialized countries is not offset by a reduced demand for the same raw materials by the old industrialized countries. The reduction might occur, however, if these countries are unable to replace their lost export markets. With a greater demand for raw materials, the purchasing power of the countries that produce them would increase, and they might be able to import more manufactured goods.

The shift in the import structure will undoubtedly affect the export of the old industrial countries, in our case the European countries. More than half of the exported goods manufactured in industrial Europe found their markets in non-European countries. In spite of the fact that this export was already very diversified, one can assume that a major part of it will be influenced by the new industrialization of the rest of the world. The European countries will, therefore, be faced with the task of adjusting their production and foreign trade to the new situation.

Theoretically it can be assumed that the increased industrial production and the consequently increased total income and total standard of living of a country would eventually lead to an expansion of international trade while the structure of this trade is changing. Thus the rapid growth of industrial production throughout the world should stimulate international trade.

The statement that trade between industrial nations is greater than between agricultural nations or between industrial and agricultural nations has often been made.⁷ It can be pointed out that until the first World War imports of industrial products grew approximately in the same proportion as manufacturing expanded.⁸ (This trend was interrupted as a result of an increase of protectionist policy which prevailed about 1890 in the United States, Germany, France, and Italy.)

The relationship between production and import was disrupted by the events following the first World War. A drastic tightening of import restrictions of all kinds during the 1930s was responsible for this change in the field of manufactured goods. While production of manufactured goods in many countries was steadily increasing, the import of industrial products did not follow this expansion; on the contrary, it fell in several instances below the level reached in the 1920s. Production in Germany reached a high level under the Nazi armed economy; this has, of course, not been reflected in increased trade. And

⁷ "Economic development of new areas means an increase in the capacity of their peoples to produce and to consume. This may be expected, on the basis of past experience, to bring a great increase in international trade, if political conditions are favorable." Eugene Staley, *World Economic Development* (Montreal, 1944), p. 22. See also National Planning Association, *America's New Opportunities in World Trade*, p. 15.

⁸ A forthcoming study of the League of Nations on "Industrialization and International Trade" contains interesting figures on this point, and discusses especially a deviation from the observed tendency about 1890 as a result of a growing policy of protection.

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the enormous rise of industrial production in the Soviet Union while her import fell below the 1913 level should also be mentioned. In the United States foreign trade also, failed to keep pace with the rapidly growing production. Thus, while it can be stated that in normal times imports of manufactured goods tended to be stimulated by expansion of industrial production, such a tendency may be checked or nullified by restrictive commercial policies, currency disorders, or by political developments.

The effects of industrialization on British trade was examined by A. J. Brown,⁹ whose findings may serve as a guide for some assumptions of the effects of the present and future industrialization on the European trade. According to Brown's analysis, British exports (revalued at 1913 prices in million £) to Germany, France, Belgium, and the United States went up from 42 in 1860 to 78 in 1873, and to 117 in 1913. British exports to Latin America and to the Empire increased during the same years from 57 to 83 and to 191. The postwar figures are: the first group took (in million pounds sterling) 86 in 1929 and only 64 in 1937, whereas the figures for Latin America and the Empire were 234 in 1929 and 200 in 1937. By 1937 the four industrialized countries were buying only 27.5 per cent as much as Latin America and the British Empire against 60 per cent in 1913. The rapidly industrializing countries continued to increase their imports from Great Britain only until 1913, a fact which does not seem to confirm the repeated statement about the growing trade between industrialized countries.¹⁰ A. J. Brown made yet another

⁹ *Industrialization and World Trade* (London, 1943), pp. 60–62.

¹⁰ The League of Nations study on "Industrialization and International Trade" contains figures for a large number of countries. The British shipments to Central and Western Europe (Austria-Hungary, Belgium, Denmark, France, Germany, Italy, Netherlands, Norway, Portugal, Spain, and Sweden) increased

interesting observation. The total real national incomes of Belgium, France, Germany and the United States increased in the period 1873–1913 probably by about 170 per cent, while their total real imports from Britain rose only by about 50 per cent. The countries of the second group probably doubled their real income and British real exports to them were more than doubled. “Demand for British exports rose three or four times as fast, in relation to total purchasing power, in the nonindustrializing as in the industrializing countries.”¹¹

Even before 1913 the increase in the export of Great Britain—the oldest industrial country—resulted much more from the expansion of her trade with countries producing primary products than with industrializing countries. The purchasing power of countries with prevailing primary production was stimulated by the growing demand for their goods, due to the expansion of industrial production in countries other than Great Britain and also by the import of capital from Great Britain.

The examination of the development of British exports indicates a further qualification of the general tendency that imports of manufactured goods are augmented by expansion of manufactures. Experience shows that during the first period of industrialization the import of manufactures grows. As industries are developed and diversified, their competitive ability against imports is strengthened, while at the same time the

from the £69 million of the 1891–95 average to £143.7 million as the 1911–13 average, or by 108 per cent; to the United States, from £24.9 million to £28.9 million, or by only 16 per cent.

The shipments to all other countries (predominantly agricultural and mining) rose from £133.1 million to £315.7 million or by 137 per cent. The exports to Central and Western Europe increased in the period 1876–80 to 1911–13 by 115 per cent, but the exports to the second group during the same time went up by 175 per cent (to the United States by 46 per cent).

¹¹ A. J. Brown, *Industrialization and World Trade*, p. 61.

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tendencies to seek protection increase and ultimately find public support.

The industrialization of European countries that were poor in raw materials and had an increased demand for foodstuffs, and, moreover, the expanding demand of the United States for raw materials and for tropical products had multiplied the export of raw materials and foodstuffs from countries producing primary products. The economic situation of these countries was now improved, and they, in turn, drew greatly increased imports from the old industrialized countries. This would, however, not be true of the industrial development of countries using their own raw materials (for instance, cotton for the cotton industry in Brazil, wool in Uruguay) ¹² and at the same time exporting foodstuffs. In the future, the newly industrializing countries will probably build industries for which most of the raw materials are locally available. Therefore, we can hardly assume that the industrialization of the overseas agricultural and mining countries will increase the national income through purchases of raw materials in other countries, in order that these in return may become greater importers of manufactures of the old industrial countries.

The new industrialization, and its impact on the old industrial countries, will not necessarily follow the pattern of the years before 1913, even if we disregard obstacles caused by commercial policy or other reasons. The composition of world trade will undergo important changes. It is expected that the traditional type of exchange of manufactured goods for primary products will decline. As economic development progresses throughout

¹² Argentine's industries used in 1937, 71.8 per cent of domestic and 28.2 per cent of foreign raw materials. Felix J. Weil, *Argentine Riddle* (New York, 1944), p. 274.

the world, the new adjustment will be possible only by a further specialization of production. More than ever will the production of industrial and agricultural specialties be important for international trade. The increased industrial production and even the improved standard of living will not automatically result in an enlarged international trade, although a basis for it should be provided. The objective of maintaining and further increasing international trade will demand a policy toward expansion of world economy. The situation created by present and future industrial expansion will require great adaptive ability on the part of the old industrial countries. The economic development of new areas inevitably offers dangers along with opportunities to them. "The net effects of these developments upon any particular country of advanced industrialism will depend upon the accidents of geography and history . . . for the way in which the established industrial area reacts to the new situation."¹³

The conclusion that the European countries have to adjust their production and export to the economic development of new areas is logical and not new; to carry out this adjustment requires a great economic flexibility and a dynamic spirit of the whole economic policy. We may quote a pertinent statement by A. Loveday, written in 1931 and referring to British trade:

It is on these new and growing industries that the prosperity of highly industrialized countries must ultimately depend. The future lies with the countries whose whole economic organization is the most mobile, with those which have the imagination to foresee future needs, the courage to scrap the obsolete plant and the skill to adopt and adapt new inventions.¹⁴

Those are the directives to be followed by the European

¹³ Eugene Staley, *World Economic Development*, p. 22.

¹⁴ A. Loveday, *Britain and World Trade* (London, 1931), p. 170.

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countries when they attempt to carry out the necessary adjustment. The burden of the task will depend on the degree of international cooperation and economic coordination. Economic developments would be greatly facilitated if the more important countries could be induced to consider the principle of comparative advantage as a guide for their programs. There is an urgent need for concerted action, if a great overcapacity in various industries is to be avoided.

Expansion of world production should certainly promote welfare everywhere and also greatly stimulate international trade, the structure of which should follow the changing course of industrial development. Yet government as well as business must decide upon a bold action. Only through a quick, far-reaching adjustment of production and through an appropriate foreign trade policy can a new equilibrium and increase of trade be achieved. Old plants and old and outworn economic enterprises—and even new industries with high-production costs—should be scrapped along with old and outworn ways of thinking. Determined action of this kind would guarantee that expanding production would lead to an expansion of international trade and would avoid the danger of further maladjustment, trade restrictions, and eventually economic warfare. The first thing—and this should be done immediately—is to make an itemized census of the world's manufacturing capacity by countries, showing the development of individual industries during the last decade and their potential market. Special committees for each industry, established at an international organization, should examine the situation in all possible details. Their findings would enable the government and the business community to appraise future possibilities, would serve as a warning against further future expansion, and would also lay a basis for the coordination and cooperation of national programs.

CHAPTER EIGHT

INTERNATIONAL ASSISTANCE IN RECONSTRUCTION

THE GOVERNMENTS of the European nations proclaim the need for building a new, a better Europe. Their economic programs all agree on some substantial objectives: to improve the standard of living; to provide full (or high level) employment; to introduce a comprehensive system of social security; and to speed up the development of the retarded regions. These programs reflect what might be called the general economic aims of the United Nations. Up to this time, however, no detailed program has been made public to indicate how the respective governments intend to achieve their objectives. It is certain that the situation of the European continent will be more difficult than that of most of the other parts of the world: the economy of the better part of the Continent has suffered great physical losses resulting from war and the many changes in the overseas markets make the prospect for export of some goods uncertain. The changed economic and financial position of Great Britain ¹ will be of special importance. Furthermore, the economic policy applied toward Germany and the future economic structure of that country will have direct and indirect effects on the economic development of Europe.

The various programs are agreed on the importance of an

¹ According to the principle of conservation of purchasing power, the income which Great Britain lost from overseas investments accrues automatically to countries repatriating the investments. This income will not, however, be put to the same use, especially in the purchase of foreign goods. Only a fraction of the amount will reach the foreign markets, and that in a roundabout way.

expanding economy. Their objectives could be achieved by widening exports in the old established markets, by building up trade with new markets (for instance, the Soviet Union), by developing the intra-European trade, and, finally, by developing domestic markets. All these possibilities will probably be tried. Europe will realize that she must be the one to adapt herself to changes in other continents because her economic structure is the more complex and also the more vulnerable. The fact that such adjustments will have to be carried out by countries in great need of postwar rehabilitation and reconstruction will make it more difficult for them. It may be countered that this new orientation in production and trade falls within the program of general postwar reconstruction; but scarcely anyone will deny that, in ability to carry out all these adjustments, there is a great difference between countries devastated by war and those which need only to adjust war production to peacetime needs.

The necessity of achieving the required adjustment in time, and of moving toward coordination of the European economy with the rest of the world is of such eminent importance that it should induce the United Nations to work out a common economic program for Europe. This is doubly essential because the political set-up of Europe will have been greatly changed. The mistake of the Versailles peace settlement in slighting economic questions should not be repeated. The magnitude of the postwar reconstruction alone is such that Europe will be desperately in need of assistance from outside. The plan for rehabilitation and reconstruction should be conceived as part of a far-reaching long-term program. Action should not be delayed, because there is danger that the moment most appropriate for cooperation—the time right after victory—may be missed. The United Nations

would be well advised to establish immediately a standing European economic committee entrusted with the task at first of a thorough analysis of the chief economic problems of Europe.² Such a committee, working in close cooperation with United Nations organizations, should then suggest the most appropriate policy for a speedy reconstruction. The task is great and must be attacked boldly and in time.

The United Nations, in an attempt to prepare a basis for economic postwar cooperation, have already started organizing international action in several fields. The United Nations Relief and Rehabilitation Administration (U.N.R.R.A.) was set up in November, 1943. Its sphere of operation is rather limited and so are the funds at its disposal. This agency is to organize and provide relief for member countries which were occupied by the enemy. (As an exception, its action was extended in a limited way to Italy.) The U.N.R.R.A. will be concerned with rehabilitation only so far as, in effect, it forms a part of relief, and when, without U.N.R.R.A. assistance, relief and recovery could not get under way. It was expected that the policy and the operations of U.N.R.R.A. would ultimately be coordinated with the long-range policy of reconstruction. Not much has been completed in this field, so far.

The funds at the disposal of U.N.R.R.A. (1 per cent of the national income of member states whose territories have not been occupied by the enemy) will amount to \$2-2.2 billion. The share of the United States is \$1,350 million. We do not need elaborate estimates to determine whether this amount will be sufficient. It is supposed to meet not only the needs of Europe

² Walter Layton recommends devising a five- or ten-year economic plan for Europe, which would create a better balance of economic status and consequently also of political power. *How to Deal with Germany* (London, 1944), p. 3.

but also those of China and other parts of Asia, and Europe will not, therefore, receive more than half of the total amount. Even if we take into account that several countries—France, Belgium, Netherlands—are prepared to pay for their relief supplies in foreign exchange, the amount at present available to U.N.R.R.A. will prove too small.

Perhaps some indication of the exigencies that will arise after the war can be obtained from the experiences of the last war. According to League of Nations calculations,³ continental Europe appears to have imported during the years 1919 and 1920 about \$17.5 billion worth of goods from overseas, against an export of only \$5 billion. To meet the import surplus more than \$5 billion was provided from loans and disinvestments (\$1 billion from expenditures of the American and British armies), and \$2.5 billion from various invisible items.

The devastation caused by the war and the exhaustion of the continental economy will be incomparably greater than after the first World War; and greater, therefore, will be the need for imports from abroad. Countries which during the last war were neutral (the Netherlands, Denmark, and Norway) will this time be in want of assistance to restore their economies. The figures we have cited refer to continental Europe without Russia. Measured on the expected magnitude of the real need for relief and rehabilitation, the possibilities given to U.N.R.R.A. by its status and actual financial strength are indeed very limited, and its activity, though certainly highly important, can only be regarded *as the beginning of any real action toward the economic reconstruction of Europe.*

Sometimes it is said that the need for financial assistance of the

³ *Europe's Overseas Needs, 1919-1920, and How They Were Met* (Geneva, 1943), pp. 22 ff.

European Continent will not be so great as generally expected because a number of countries possess large monetary exchange (gold and balances in dollars), the amount of which has increased during the war.⁴ This is correct for the neutral countries. The disclosed gold and foreign exchange reserves of Switzerland increased from \$631 million at the end of 1939 to \$1,035 million at the end of September; those of Sweden went up at the end of 1939 from \$385 million to \$529 million at the end of 1943, those of Portugal from \$60 million to \$644 million. (The monetary reserves of Spain reached \$105 million at the end of June, 1944.) So the neutral countries, whose economies have not suffered from war in any way comparable to the case of countries occupied by the enemy, will be able to finance their own import needs, and even to grant some assistance to other European nations.

The Western European countries succeeded in saving a substantial part of their prewar gold and foreign exchange holdings. France is reported to have had at the end of September, 1944, \$2,000 million (against \$2,709 million at the end of 1939); the Netherlands \$500 million (against \$692 million); while Belgium registered an increase from \$609 million to \$750 million. These nations will be able to pay for their relief and rehabilitation supplies. The substantial holdings, however, must not lead to any premature conclusions as to real financial strength. It must be remembered that these countries will not only be in urgent need of relief supplies but that they will also require a complete restocking of raw materials and of a great part of machinery and rolling stocks. (It has been estimated that France

⁴ See National City Bank of New York, *Bulletin*, Aug., 1944, p. 94; Foreign Trade Capital Movements, and International Reserves," *Federal Reserve Bulletin*, Nov., 1944.

will spend in 1945 around \$700 million on supplies needed from the United States.) And it will take time before they are in a position to start exporting on a larger scale. They will have to use all their foreign funds in order to rebuild their economies, and in addition they will need foreign credits, as has already been indicated by the \$100 million loan to the Netherlands recently arranged in New York.

The situation of the countries of Central and Eastern Europe is, of course, much worse. The gold and foreign exchange reserves of Czechoslovakia, Poland, Yugoslavia, and Greece are negligible, if compared with their requirements. And nobody knows how much gold they will obtain from Germany. Although U.N.R.R.A. is not supposed to extend its activity to Hungary, Bulgaria, Rumania, and Austria, these countries too will be in great want of foreign assistance. Their economic rehabilitation will be of substantial importance to the economic consolidation of this part of Europe. How great the need of Italy is, we have already seen. She will get some assistance from U.N.R.R.A. (not more than \$50 million) and from the United States, redeeming in dollars the lira notes spent by the Allied armies. However, this is obviously in no proportion to the assistance from abroad which will be required for the economic restoration of Italy, who has suffered worse in this respect than is generally assumed.

Germany really has no place in this discussion, as certainly no United Nations agency will take over the care of her people or her economy. Nevertheless we can visualize a situation of such destruction and exhaustion that the Allies may be obliged for reasons of safety, alone, to help her on a limited scale.

Altogether, the needs of the European Continent will be much greater than after the last war, and it is highly desirable that the task ahead should be clearly seen and attacked in time by

international agencies. Very appropriate is the following comment of the study of the League of Nations which refers to the difficulties after the last war:

The effects of the failure to face the problem of Europe's post-war requirements of raw materials and essential manufactured goods with any imagination or courage comparable to that shown in furnishing food relief, were no more local than transitory. The penury of European countries induced them to husband their resources by quantitative restrictions on exports and imports and the fear of their lowered standard of living induced others to refuse to accept their products. Commercial policy was driven from the outset down the wrong road and never found another.⁵

The United Nations conference in Bretton Woods in July, 1944, proposed to establish two institutions: an International Monetary Fund and a Bank for Reconstruction and Development. If created in time, these instruments will help in consolidating the situation in Europe, but their operation, as proposed, might not suffice in all cases. The situation of a number of countries in Central and Eastern Europe will be similar to—and in most cases rather worse than—that of Austria, Hungary, or Bulgaria after the last war. In order to facilitate economic and financial reconstruction, something like the League of Nations loans might be advisable. Such global loans should be coupled with a well-conceived general program of reconstruction and development, and more attention should be devoted to international as well as national economic problems than was done in the case of the League of Nations loans. Should the status of the Bank for Reconstruction and Development not cover this kind of loan, there would still be ample opportunity to add the necessary provisions or to organize some other machinery.

⁵ *Europe's Overseas Needs*, p. 48.

Broadening the activities of the United States Export-Import Bank and increasing its lending power would enable it to provide short-term and medium-term credits to finance American exports.

It has recently been stated that the thesis of Europe's need of large capital imports after the war is not correct.⁶ The example of German development after the last war is taken as proof that Germany accomplished her recovery during the twenties chiefly by saving and by hard work. There is no doubt that currency stabilization cannot be achieved and maintained without an appropriate internal economic policy. But the situation of the devastated countries in Europe can hardly be compared with that of Germany after the last war; she started the period of reconstruction with her economic machinery on the whole intact and within a Europe quite different from the one we shall have this time, and it would be difficult to deny that the rapid modernizing of German industry was made possible only by the help of foreign credits.

Furthermore, the time factor has to be considered. The more quickly the economy of the exhausted countries is put back to effective work, the better the whole reconstruction program will progress. It is needless to mention how long it would take before the people's savings could provide capital for rebuilding the destroyed economy, say, of Poland or of Yugoslavia. And it should be clear what would happen in the meantime not only to these countries but also to their neighbors.

It would be of great value for the orientation of the European countries themselves if the program of international monetary and financial assistance could be accompanied by a mutually approved program setting forth the main directives in the field

⁶ Dr. L. A. Hahn, "Capital Is Trade at Home," *Social Research*, May, 1944.

of foreign trade policy. U.N.R.R.A. has collected valuable figures on the estimated relief exigencies of the European nations. It would be of even greater importance—though the task is more difficult—to prepare some kind of inventory of the European economy, an inventory that would include the status of industries and the possibilities of putting them back to work; that would analyze agriculture and its immediate needs; and, finally, that would give a picture of the transport situation and its difficulties. On this basis it should be possible to discuss a long-range program of rebuilding European economy.⁷ A program of this kind is necessary as a guiding policy in the transition period; it should provide an atmosphere of mutual confidence. Though it is not our task here to deal with the transition period, it should be emphasized that many measures taken then will have major significance in the long-range programs.

Whereas the United States, Great Britain, Russia, and Canada were able to prepare for peacetime reconversions and to make their plans on the basis of a thorough knowledge of their own economies, by which they were able to estimate coming developments, nothing of that sort was possible for the occupied countries. Here the government's role in economic life will be much more extensive than ever before. Many of the wartime controls must remain in force for a number of years. Nobody can tell at present which of these government controls will be temporary and which will form an established part of an economy under increased state control and interference.

Despite the great damage done to plants and factories, the

⁷ The report of the National Planning Association, *America's New Opportunities in World Trade*, p. 53, estimates the range of \$40-70 billion as the probable limit of European reconstruction capital needs. It assumes that perhaps half of this can be met locally and perhaps one half of the remainder, or one fourth of the total, will be required from the United States.

difficulties of setting European production on its feet should not be insurmountable. We know how very efficiently the modern economic system can meet new demands if the appropriate conditions are present. Europe will depend on foreign assistance on a large scale. Her reconstruction, including reorientation of her production where needed, should be an integral part of a comprehensive plan of international economic cooperation. The greater the amount of real assistance given to Europe during the period of reconstruction, the shorter this period will be. The coordination of European economy with the main trend of world economy, coupled with a real and sincere cooperation between Europe and the rest of the world and among the European nations themselves, would help to ensure that the policy followed in rebuilding Europe will take the right direction.

CHAPTER NINE

ECONOMIC INTEGRATION OF EUROPE

THE PAN-EUROPA SCHEME

A UNITED STATES of Europe comprising one large economic unit has repeatedly been proposed. The economic developments of the United States are often cited as an example of a favorable division of production that can be achieved within a large unit and that can lead to an increased domestic market and a rising standard of living. Though the idea of the large unit has much to recommend it on purely economic grounds, nevertheless Europe cannot be compared off-hand with the United States. Here the present economy has emerged in modern times within one unit, whereas Europe comprises a number of units historically developed under different circumstances. To put them together now would create difficulties which cannot be easily overcome. Should the present technological trend toward large-scale production for a big market continue, then a tendency to either large units or to a more liberal commercial policy might be expected. On the other hand, the trend toward controlled economy would not support the creation of big units, for it would make the administration less flexible and difficult.

Regardless of its immediate utility or likelihood in the near future, the formation of the United States of Europe does not constitute by itself a solution for Europe's position in the world economy. Europe, as a whole, is dependent upon the import of food and raw materials from other territories, and, conversely,

non-European countries have bought about half of all the exports of manufactures originating in industrial Europe. Domestic employment on the European Continent is dependent on the import of food and raw materials. This situation cannot be met by the creation of a European unit, unless a policy of self-sufficiency, with an attendant decline in the standard of living, is advocated. Even the development of synthetic products and of new materials and a much wider use of timber and various plastics, have not changed this situation basically, particularly if we expect from them a high level employment and rising standards of living.

As a matter of fact, the supporters of Pan-Europa will not find much help for their plan in the recently published "constitution" of the Pan-Europa movement. It does not offer any concrete economic program.¹ In the extensive literature this writer has found no real economic analysis of the problem, which very often is dealt with in a rather formal way.

In spite of a widespread belief to the contrary, the possibilities of creating such a European unit after this war seems even more remote than ever. Only if formed in response to a spontaneous demand by the nations concerned could it offer any hope of success. An atmosphere of complete political confidence, and freedom from fear, as well as the abatement of exaggerated nationalism and narrow-minded economic egoism are prerequisites. People will have to believe and practice democracy in its true sense before real progress in this direction can be expected. It would not be realistic to count upon a United States of Europe in any program of reconstruction. Even if the idea has economic

¹ See *Draft Constitution of the United States of Europe* (New York, 1944), Report of the Pan-European Conference, New York, 1944; A. Weinfeld, *Towards a United States of Europe* (Washington, D.C., 1942).

merits, political difficulties in and outside Europe make its realization impossible. And how can any sober-minded person expect that nations newly emerging from the terrible ordeal thrust upon them by Germany would agree to form a Pan-European unit with that country?

Other suggestions attempt to foster the economic integration of Europe by somewhat formal measures. Here belongs a plan to establish a European railway (and airway) corporation to achieve a uniform administration of the entire continental railway system. Even if we disregard the political factors militating against such a construction, the managerial problem would involve a personnel of about four million men of many different nations. Efficient operation would require a large degree of autonomy for the national railways, which could easily make international transportation subordinate to national and political considerations and requirements. A railway system becomes of necessity unified if the several national economies are integrated; the process in reverse would never be successful.

The opinion has also been expressed that the giant trusts formed by the Germans and spread throughout Europe should be maintained as such and internationalized. Similarly, the continuation of the German-European cartels was considered a good device for the economic unification of Europe. According to this view, the trusts should be owned by an international agency with shares allotted to the participant states; the German shares should be used as reparation payments. The international agency, directly dependent on an association of nations, should administer these monopolistic combines. Such a scheme would inevitably lead to a system of great European monopolies, very few of which could be justified on economic grounds. When, as an example of combines that should remain intact, the Hermann

Goering Werke or the I.G. Farben are cited, little can be said to prove that they represent either a vertical concentration or an economically and technologically useful amalgamation. The outcome of this proposed international agency may well be a regulated Pan-European economy, which from the very beginning would contain dangerous seeds of future conflicts.

These and other proposals attach too great an importance to the external forms of economic unification which should serve as instruments to bring about a real economic integration. Yet they do not touch the heart of the problem.

Although we do not consider a United States of Europe the solution to the real problem, neither do we advocate a return to the economic *status quo* before the outbreak of the war. The need of economic, particularly industrial, reorganization, resulting from the physical destruction of war in large areas, and the need of foreign assistance for economic reconstruction in general, creates an opportunity for large-scale planning.² "Neither economic nationalism nor feelings of revenge nor short-term interests of investors must interfere with the supreme goal of reintegrating industrial Europe (and the continent as a whole) within itself and with the wider world."³ Nobody will deny that

² Sir Walter Layton suggests that the European nations of their own free will and determination establish a European Association to which they would be prepared to entrust some of their most vital interests. Such an organization would set up a European General Staff to take care of order and security. It would, furthermore, establish a Charter of Liberties written into Europe's regional pact. And, finally, it would deal with certain economic matters, especially with the control of Germany's war industries, the breaking of her economic hold on Europe, and the economic development of the backward states. It emphasizes that the rest of the world is entitled to ask the countries of Europe to set up a European organization to deal with these three requirements and to assign to it sufficient authority to carry them out. *How to Deal with Germany* (London, 1944), pp. 23 ff.

³ Adolph Lowe, "The Trend in World Economics," *The American Journal of Economics and Sociology* (1944), p. 431.

before the war the European economy was not organized along the line of comparative advantage and that it has not followed the best pattern of division of production even within Europe. High-cost agricultural production was expanded in the advanced industrial areas, while the agricultural exporting countries suffered from a lack of outlet abroad.

Plants of equally high-cost industrial production were erected in the depressed regions of Eastern and Southeastern Europe and in many other countries. War itself has probably brought about a further maladjustment in the European production. But Europe will be unable to recover and to adapt herself to the new world situation if she continues the policy of economic nationalism of the thirties. It must become clear to the European nations that they cannot demand a policy of world trade expansion while they themselves practice economic restriction within the Continent. It should be evident that a Europe divided into watertight economic compartments cannot achieve a uniform prosperity. The policy of "Beggar your neighbor" is nowhere more unfortunate than here.

It should also be understood that economic and political considerations require a leveling of the sharp differentiation between the wealth of Western Europe and the poverty of Eastern Europe. The only constructive way to reach this goal is to develop the retarded Eastern and Southeastern areas. Even before 1913 these areas were characterized by the following: an export surplus of agricultural products for which Europe was the natural market; a lack of capital that slowed down industrial expansion and prevented any notable improvement in primary production and the construction of public utilities, especially of transport facilities; a relative overpopulation in agriculture. "In Southeastern (and also in Eastern) Europe a considerably

larger population is employed in agriculture per unit of arable land than in Central—and, of course, Western—Europe, with a much lower average yield, and with much less capital available; the result is clear—a low standard of living and relative overpopulation.”⁴

Without a well-prepared program of economic development for this whole area there can be no economic consolidation and integration of Europe. And now when plans are being prepared for the development of China, India, and other similar regions of the world, nothing is more appropriate than to include this section of Europe, where good progress can certainly be achieved in a shorter time than in some of the other countries.

A REORIENTATION OF EUROPEAN AGRICULTURE

A fundamental reorientation of European agriculture is a necessary condition to an economic integration of the Continent. The adjustment of European agriculture to the new situation overseas had not been carried out beyond the border of Germany. The “steel and rye” tariff of 1879 ushered Germany into the era of a policy of increasing protection of agriculture which culminated in the policy of planned self-sufficiency in food during the thirties.⁵

Other industrial countries (Italy, France, Czechoslovakia, Austria, and even Switzerland) also introduced high protection for agricultural products, supporting these measures by various reasons. The following figures compare the price of wheat per

⁴ See the author's *The Danube Basin and the German Economic Sphere* (New York, 1943), p. 234; and see also D. Warriner, *Economics of Peasant Farming* (London, 1939), p. 9.

⁵ See Alexander Gerschenkron, *Bread and Democracy in Germany* (Berkeley, Calif., 1945).

bushel (January, 1936) in surplus-producing countries (Group I) and deficit-consuming countries (Group II).⁶

<i>Group I</i>		<i>Group II</i>	
<i>Country</i>	<i>Price</i>	<i>Country</i>	<i>Price</i>
Argentina	\$0.93	France	\$1.55
Australia	0.99	Austria	1.85
Canada	1.01	Czechoslovakia	1.97
United States	1.06	Germany	2.29
		Italy	2.47

Though the price in the Danubian wheat exporting countries was a little higher than the price of the overseas wheat, it was still very substantially below the one in the high-cost producing countries in Europe. This picture could be supplemented by comparing prices of many manufactured goods in the European industrial countries and in the depressed agricultural areas. In the latter we would find the farmers paying much higher prices for industrial commodities than the farmers in Central and Western Europe. The policy of high protection—implemented not only by tariffs but to an even greater degree by numerous quantitative import controls—was directly responsible for these price developments in Europe. The result was to divide Europe into at least two groups and to prevent the economic integration that would assure a higher level of living throughout the Continent.

A fundamental change in agriculture is one means of expanding the inter-European exchange of commodities and of providing a regular market for agricultural exports from Eastern and Southeastern Europe. It is in agreement with the important recommendations of the United Nations Food Conference at

⁶ *The Midcontinent and the Peace* (Minneapolis, The University of Manitoba and the University of Minnesota, 1943), p. 23.

Hot Springs in 1943, which set forward some basic principles for agricultural and food policy. Great emphasis is being laid on improving the standards of nutrition; if this were done, it would automatically lead to an increase in agricultural production as a whole. The program would fit in very well with the requirements of a shift in production from energy foods to protective foods (meat, dairy products, eggs, vegetables, and fruits)—a change which is badly needed in European agriculture. In this direction there is much to be done throughout the Continent, although some progress, particularly in Western Europe, was achieved during the interwar period. The reorientation of the Danish agriculture in the last decades of the nineteenth century serves as a very good example. But such a policy can only be carried out successfully if there is a firm determination to cut agricultural protection radically, and, by so doing, to increase world trade.

The proposals contained in *The Midcontinent and the Peace*, a report prepared under the auspices of the University of Manitoba and the University of Minnesota, move in a similar direction though dealing chiefly with the relation between the overseas agricultural producers and Western and Central Europe. The report states that to achieve freedom from want "requires a most drastic reorganization of the agriculture of the countries of Western Europe." This apparently includes also the Central European nations. Such a policy constitutes an important step toward a better-working world economy. Cheaper food can be provided for the peoples of Western Europe, a move by which wheat producers in Argentina, Australia, Canada, and the United States would greatly benefit. The concrete proposal suggests that Canada, the United States, and Great Britain, with the cooperation of Russia and in concert with the countries of

Western Europe, shall make arrangements whereby the Western European countries, including Great Britain, undertake to receive within a specific period, perhaps fifteen years, certain agricultural products (wheat, barley, pork, and lard), from producing countries in specified maximum amounts. The producing countries would assist in the reorganization of European agriculture in order to enable Europe to import larger quantities of such agricultural products. The countries of Western Europe should produce more milk, butter, cheese, eggs, meat, fruits and vegetables, and less wheat, barley, pork, and lard. The producing (exporting) countries would also undertake to encourage necessary reductions in their own tariffs to permit the countries of Western Europe to pay for the larger quantities of agricultural products they will want to buy. The report mentions tariff reductions on many light products and handicrafts that are special features of European production.⁷

Although the proposals are certainly correct in principle, they need further elaboration and qualification, especially on two points. It is not realistic to assume that the European countries will change the structure of their agriculture (in any case, a long-range operation), without the assurance that, after the change has been made, countries supplying them with agricultural products will be prepared to buy manufactured goods regularly in exchange. Tariff reductions which could be altered at any moment will not do; long-term treaties are indispensable. Furthermore, these proposals consider the Western and Central European countries mainly as a market for overseas agricultural products and disregard almost entirely the fact that Western and Central Europe have been the most important market for agricultural products from Eastern and Southeastern Europe.

⁷ See *The Midcontinent and the Peace*, pp. 22 f.

The problem cannot be solved without taking into consideration the needs of the depressed areas. The mistake of the thirties, namely, the closing of European markets to the Danubian countries, which pushed them directly into a tight German economic embrace, must not be repeated. "In the past these countries have been the victims of the fluctuations of the world market and of the policy of autarchy which resulted from them."⁸ Before Europe's economy can be coordinated with the world economy it must be coordinated and integrated within itself. And the problem of security in Eastern Europe is inseparable from that of Europe as a whole.⁹ However, it should be pointed out that Europe's net export of foodstuffs covered less than a quarter of industrial Europe's net import of foodstuffs (including Great Britain), the share of Eastern Europe being substantially less. A sufficient market is left for imports from overseas.

Though the program of a new orientation of production should be applied to European agriculture as a whole, it should be remembered that the countries where high prices prevail have a relatively high level of efficiency and their farmers have superior technical skill. They can therefore more easily adapt themselves to the production of protective food and are better prepared to make the necessary readjustment than are the peasant countries of Europe. The latter will be greatly dependent upon outside aid, but they in turn will be able to supply the more progressive countries with the cereals and fodder crops needed for expanding the production of cattle, pigs, and poultry. Yet agricultural production in the retarded region must be better balanced. Cereals have occupied too great a place in some sec-

⁸ Royal Institute of International Affairs, *Agrarian Problems from the Baltic to the Aegean* (London, 1944), p. 62.

⁹ M. Momtchiloff, *Ten Years of Controlled Trade in Southeastern Europe* (Cambridge, England, 1944), p. 68.

tions; the lack of capital was among the factors responsible for this.¹⁰ As a first step a reduction of cereal crops in favor of fruit, vegetables, and fodder for livestock is to be recommended.

It should be understood that it will be harder to rebuild agriculture in Eastern and Southeastern Europe than to reorient agriculture production in Western and Central Europe. Great advances in irrigation, soil conservation, and the consolidation of peasant properties will be required in order to accomplish it. All that is, of course, a long-range program which cannot be carried out overnight. But the development as envisaged would step by step abolish the great poverty prevalent in some regions. International cooperation, financial and technical assistance, are necessary. A comprehensive program would include greater intensity and diversification of production, the commercialization of agricultural marketing, financing, transport, and proper education. The very low level of domestic food consumption and the extremely low yield compared with other European countries illustrate both the possibility and the need of intensifying production of the present type of crops.¹¹

The use of farm machinery has been very low and the consumption of artificial fertilizer nearly negligible. (It has been reported that in an attempt to augment the food supply the Germans used intensified farming practices, particularly in Western Poland and Rumania, inducing the peasants to use farm machinery and fertilizers.) In the production of protective food this area has been far behind Western Europe, devoting to it less than one seventh of its agricultural soil as against one third in the West. There is room for a good deal of diversification.

¹⁰ *Agrarian Problems from the Baltic to the Aegean*, p. 73.

¹¹ For figures see the author's *The Danube Basin and the German Economic Sphere* (New York, 1943), p. 232.

So long as these countries do not possess other exportable commodities they will remain dependent upon agricultural exports to obtain their vital imports.¹² In addition to grain and foodstuffs the export of agricultural production will consist of tobacco, eggs, fruit and vegetables, poultry, dairy products, perhaps vegetable oil (or vegetable-bearing crops) and lard. The bulk of the exportable surplus will have to be sold to the old natural markets—Central Europe, Germany, Italy, Belgium, Holland, Spain, and the Scandinavian countries.¹³ It is evident, therefore, that the agricultural policy of Western and Central Europe must be such as to make imports from the depressed areas in Europe possible. This trade will be a prerequisite for the improvement of the economic situation of Eastern and Southeastern Europe, as well as for expanding intra-European trade, and it will be a good beginning toward gradual economic integration.

With regard to those regions which after 1939 became a part of the Soviet Union, the pressure of agricultural surpluses will be reduced. This applies to Bessarabia, the eastern parts of the Poland of 1939, and the three Baltic States. The Soviet Union may absorb their surpluses; it will mean a slight reduction in the export of cereals, fodder, and animal products. On the other hand, some industries previously supplying these areas may lose their markets here.

¹² Royal Institute, *Agrarian Problems from the Baltic to the Aegean*, p. 62.

¹³ See Momtchiloff, *Ten Years of Controlled Trade*, p. 68. Karl Brandt (*The Reconstruction of World Agriculture*, p. 386) stresses the fact that the real economic problem of these countries will be to find a sufficient outlet for agricultural surpluses. The only area which can possibly absorb such surpluses lies in the industrial northwest of Europe, especially in Germany. And, as Brandt states it, this nexus will not be altered, not even by radical changes in the political map of Europe or the partition of Germany into several separate states.

Any long-range reorientation of European agriculture, and especially one including an increased dependence on food imports, will only be possible if there is a justified hope for a prolonged period of peace. Otherwise the countries concerned will be very reluctant to lower protective tariffs on agricultural production. (It seems like a paradox that greater dependence on food imports in itself is a definite factor favoring peace, yet a food production on really economic terms cannot be achieved without a justified hope in peace.) A change of foreign trade policy is inevitable. Economic integration of agriculture will obviously not be identical with the complete removal of agricultural protection, nevertheless the first step in the direction of efficient help should be to reduce such protection to its level of 1913. At that time there was not such a striking difference between the level of agricultural prices in the industrial countries having protection and those on the world market.

For the orientation of European agriculture the period of rehabilitation will be of major importance. The U.N.R.R.A. will supply foodstuffs, seeds, and livestock and, as an advisory organization, will assist in the efforts to restore European agriculture. A study published by the League of Nations¹⁴ shows that after the last war it took more than seven years before the prewar intensity of European agricultural production was reached. Considering the duration, geographical expansion, and nature of the present conflict, one may expect that the agricultural position of the continent will be weaker than it was after 1918. The need for relief from overseas and for assistance in reconstruction will be of greater scope and urgency. It would only be nat-

¹⁴ *Agricultural Production in Continental Europe during the 1914-1918 War and the Reconstruction Period* (Geneva, 1943), p. 55.

ural if, in a starving world, short-term needs dictated the policy to be followed, and this could easily mean that it would aim at achieving maximum production along the existing lines without regard to the desired specialization. Yet as the *Economist* rightly comments:

To get maximum production—there must be some division of labor between the various European countries, so that, over and above immediate local needs, each specializes in the products to which it is relatively best suited. Further, a balance must be struck between Europe and world economy. . . . The coordination of world food production remains an urgent necessity.¹⁵

The U.N.R.R.A. should closely cooperate with the Commission for Food and Agriculture—the existing opportunity to plan for a coordination of world food production should be used. Germany's agriculture should be planned to fit into the whole European program. This could be done during the period of occupation, and will be of great importance to the European agricultural countries (especially the Danube basin).

During the period of rehabilitation and reconstruction there will be no lack of markets for agricultural exports, and the experience gained during this time will probably suffice to determine whether agriculture in Eastern and Southeastern Europe will really be able to compete with overseas products. If it is not, a temporary solution can be found in several ways: international commercial agreements granting certain quotas to the agricultural exporting countries of Europe; an internationally supervised preferential regime, which would be strictly limited in duration; or finally, the governments of the importing countries could commit themselves to purchase annually for a number of years definite quantities of certain products.

¹⁵ Sept. 2, 1944, p. 312.

INDUSTRIALIZATION OF THE DEPRESSED AREAS

European industry will be confronted with the prodigious task of rebuilding destroyed plants, renewing worn-out machinery, catching up with technological progress, replenishing raw materials, regaining prewar foreign markets. The difficulties of adjustment to the entirely new situation should not be underrated. It is essential to find out what changes European industry has undergone during the war. Many attempts to gather such information have been made, but it is impossible to discover which industries were dismantled, what new factories were erected and where, and what the condition of the equipment is. For example, although a half of Italy has been occupied for a year, we have not yet ascertained the real situation of Italian industry, except for the obvious facts of great destruction and dire need for help.

It is certain that the need for tools, machinery, spare parts, and exchange of new technical information will greatly surpass the requirements after the last war. If in the near future, a comprehensive and itemized survey could be prepared, by real experts, and if these data could be compared and coordinated, industrial reconstruction within each country could be planned with regard to the entire European situation. By such a process—assuming agreement is possible—a better distribution of industrial production could be attained, various vested interests of a noneconomic basis could be weakened, and the way would be open to freer trade in greater volume.

If Europe is to maintain and raise its standard of living, the industrial potential cannot be reduced but must, on the contrary, be increased. The industrialization of the retarded agricultural areas must be resumed. It is now generally recognized

that industrialization of these regions is in the common interest not only of those countries but of Europe and of the whole world. The excess of agricultural population throughout Eastern and Southeastern Europe, estimated before the war at more than twenty million and with an expected increase of seven million during the next decade, cannot be absorbed even by a much intensified and advanced agriculture. The necessity for providing an outlet for this excess was recognized during the thirties, when industrial production was increased in all these countries. Though the indices of industrial production show a considerable increase, the absolute level was still very low.¹⁶ The value of machinery per head was at most 10 per cent of that in the more industrialized countries of Europe. In Hungary, the value of industrial production per head of population was about 14.5 per cent of that in Germany; in Yugoslavia, 7.8 per cent; in Rumania, 6.9 per cent; in Greece, 5.9 per cent; and in Bulgaria, 3.5 per cent. Yet the resources of these countries, compared with those of Germany, indicate clearly that conditions for further development of industries exist.¹⁷ Mineral resources include bauxite, chromium, petroleum (Rumania, Hungary, Poland), copper, lead, zinc, and antimony, further coal, lignite, and also iron ore. Large forests in Poland, Rumania, Yugoslavia, offer great possibilities for the production of paper, furniture, rayon, and plastics. Hydraulic power represents only a small fraction of the estimated potential. It has been suggested repeatedly that a Danubian T.V.A. would foster the development

¹⁶ The index of industrial production increased in Poland from 100 in 1929 to 117.2 in 1938; 125 in Hungary; 132 in Rumania; 128.4 in Yugoslavia; 155.4 in Bulgaria; 165.1 in Greece. Royal Institute, *Agrarian Problems from the Baltic to the Aegean*, pp. 81–82.

¹⁷ See a detailed table in the author's *The Danube Basin and the German Economic Sphere*, p. 230.

of Southeastern Europe by promoting industries and transportation throughout a large part of the Danube basin.

The possibilities of development undoubtedly are here. During this war some industries have been expanded and some new ones created in parts of Poland, in Hungary, and in Rumania. While some will probably be established for war purposes only, others might be used also in peacetime. Consumption goods industries, however, have probably been stopped. "To industrialize the area is certainly a tremendous task."¹⁸ If industrialization could be carried out systematically and with mutual cooperation, the difficulties would be substantially reduced. The countries concerned do not possess enough capital to build industries; they do not have sufficient resources to resort to domestic formation of capital as did the Soviet Union during the interwar period. Foreign capital, whether as loans or as direct investment, will be required in addition to the formation of domestic capital.¹⁹ It will not always be easy to work out conditions for this cooperation of foreign capital. Some industrial equipment will perhaps be forthcoming as reparations payment from Germany, and it may also be possible to move some industries to countries where the necessary conditions exist. Germany is, for instance, a high-cost producer of aluminum. Yugoslavia, with her large bauxite deposits and great potential resources of hydraulic power, would offer a good location for this aluminum industry. In addition to financial assistance these

¹⁸ Royal Institute, *Agrarian Problems from the Baltic to the Aegean*, p. 82.

¹⁹ P. N. Rosenstein-Rodau in "Problems of Industrialization of Eastern and Southeastern Europe," *The Economic Journal*, June-Sept., 1943, pp. 202-211, puts the need of capital for industrialization for 10 years after the war at £4,800 million, half of it to be supplied by countries in Eastern and Southeastern Europe. In addition, £1,200 million will be needed for the improvement of agriculture; the bulk of that should come from domestic sources.

countries will also need technical help on a large scale. Economic development of these depressed countries, agricultural as well as industrial, will increase national income, will create new consumers for all kinds of goods, will change the structure of, but at the same time stimulate and expand, European trade. These one hundred million people represent the last big reserve of Europe's potential consuming power.

The difference between wealthy and depressed Europe must be narrowed. This can be done if national income increases more rapidly in the retarded regions than in the already advanced countries. The latter should themselves be interested in supporting plans to integrate various aspects of the economic problems of the depressed areas. They will have to assist in several ways, including the lending and investing of capital. It can be said without reserve that such investment, based on a broad cooperation, would be an investment in European peace.

REGIONAL GROUPS

To accelerate such integration, the formation of larger economic units of various types has often been recommended. The economic argument is that modern mass production requires a sufficiently large market and a full division of labor. The idea is frequently supported by political arguments: a larger economic unit would increase the economic strength of all its members, who could then build adequate defenses against aggressors. In the interwar period several attempts were made to organize regional economic units, especially in Central and South-eastern Europe; none of the plans, however, were successful in the sense that the scheme would have expanded international trade or worked toward real economic unification.

During the ten years preceding the war, when protectionism

resorted to all kinds of quantitative restrictions and especially when bilateral trade arrangements (clearing and barter agreements) were widely used, it became evident that under a full-fledged interventionist system in foreign trade policy the economic position of small countries suffered. It is obvious that in a time of relatively free trade there would be no substantial difference in the position of the small and the large countries and that there would be less demand for such larger units as customs unions or preferential regimes. In an interventionist economy the need for uniform policy could not be limited to customs tariffs but would have to embrace all important aspects of economic policy. The growth of economic planning and intervention, ranging all the way from the issuance of certain general directions to the supervision of regular business transactions, complicates further the whole nature of the problem of customs unions.

The history of the interwar period is being examined for an indication whether the record of the small states was worse than that of the large ones. Undoubtedly the development of Switzerland and Sweden can stand comparison with any other state; the Low Countries and Czechoslovakia also achieved good progress. And it has correctly been pointed out that the greater flexibility of the economic system of smaller units can offset the handicap of size, since the economy of the small state can be adjusted more quickly and more easily than that of the larger nations with complicated systems. The period between the wars does not seem an appropriate basis for a comparative study of small and large nations. Each comparison needs a special analysis and qualification before any appraisal can be made.

One assertion made in this connection is that the creation of the national states in Northeastern and Central Europe had a

beneficial effect on world trade.²⁰ Now, nobody will deny the progress achieved by these nations in many fields, and everyone will recognize the great driving power of people who have been left alone to manage their own affairs.²¹ However, the foreign trade policy of many of these nations scarcely inspires admiration. It is a truism that in the thirties the great stimulus to the foreign trade of the majority of these countries was given by the German trade drive to Southeastern Europe. Little is to be gained by a flat comparison of industrial indices. For example, an increase of 50 per cent means little in a country whose industries were nil, whereas a 10 per cent increase may mean a great deal in a country already industrially advanced. The importance and the situation of small countries must be more soberly judged. Their significance and their merits are such that they do not need assistance from statistical comparisons, even if these are made with the best intentions.

It is clear that the freer the international exchange of commodities the better the prospects of peace and the more favorable the position of the small nations. Some people expect that after the terrible experience of the Nazi occupation the nations will be inclined to form units with other nations; many, on the other hand, anticipate a wave of intensified nationalism with greater emphasis on national sovereignty.

For a formation of customs unions or economic federations two basic principles must be recognized: The first is that such a union or federation can be established only on a voluntary basis, when the nations concerned really desire it; secondly, it should provide for a better division of production and expansion of trade. World trade would remain unaffected if the formation

²⁰ V. Rundt, *The Smaller Nations in the World's Economic Life* (London, 1942).

²¹ See the author's *The Danube Basin and the German Economic Sphere*.

of an economic federation merely caused a shift of trade between countries, and the trade expansion between the members of such group was accompanied by a reduction of trade with other countries. In a customs union the new tariffs should not be higher than the average tariffs of the member states.

A beginning in the right direction was made by the negotiations between The Netherlands and Belgium-Luxembourg to conclude a customs union. These countries are largely complementary in economic character, and the necessity of reorganizing their economic life after the war will facilitate in overcoming practical difficulties that might be insuperable in normal times. The agreement will be provisional and limited to the period of relief so that adjustments can be made as required.²² The formation of federations in Central and Eastern Europe has again been in the center of discussion during the last years. Repeatedly an ambitious plan has been advanced for an economic unit to include all countries between the Baltic and the Black Sea: Poland, Czechoslovakia, Austria, Hungary, Rumania, Yugoslavia, Bulgaria, Albania, and Greece.²³ The Soviet Union took a negative attitude, suspecting that any such plan might be used to establish a "Cordon Sanitaire" against her. Regardless of the Russian view, we must recognize that the area is far from a homogeneous unit. Substantial differences exist in the standard of living and in the economic and social structure; the political and cultural differences are also great. Czechoslovakia and Austria have highly developed and diversified industries, whereas many of the agricultural countries have industrial enterprises which owe their existence only to the protectionism of the last

²² *Economist*, March 11, 1944, p. 336.

²³ A recent Plan of this sort was proposed by Peter Jordan, *Central Union of Europe* (New York, 1944).

decades. Furthermore, even such a big unit—although providing a great domestic market—could not solve the main problems of the agricultural countries within it, as it could not give them an outlet for agricultural surpluses, remove the lack of capital, or take care of the excess of agricultural population. It should not be regarded as a panacea.

Other, more modest schemes propose a Balkan union or a Danubian federation. A foremost expert on this area, R. W. Seton Watson, holds that the mutual relation of these countries can only be satisfactorily built upon federal lines.²⁴ Discussing the possibility of a Balkan union, he suggests that Bulgaria holds the key to the whole situation, thanks to her geographical position. As to the Northern Confederacy including Czechoslovakia and Poland, he regards the Austrian adhesion to it as essential for future settlement. Hungary has the key position in the Middle Danube. Transformation of Hungary from a feudal to a democratic basis, which presumes land reform, would remove the main obstacle to cooperation throughout this zone. It is very difficult to make at this moment any prophecy as to what the eventual decision will be. Although Russia is reported to be opposed to any federation here, her attitude might change after the war. Even so it will not be easy to find the right solution. On purely economic grounds we could solve the problem by grouping together countries with economic and social structure closely similar to, and perhaps complementing, each other. There are, however, many political, cultural, and national issues to be considered. Should the nations reach the conviction—as we hope they will do—that close cooperation within a federation or some other form of union is desirable, any such move ought to be

²⁴ R. W. Seton Watson, "The Zone of Small Nations in Eastern Europe," in *Agrarian Problems from the Baltic to the Aegean*, p. 34.

encouraged, assuming that it is in the general direction of expanding economy and trade.

To summarize our findings in this chapter, we believe that a greater integration of the European continental economy is indispensable. In order to achieve it, the restrictive trade policy must be replaced by a policy of trade expansion. A reorientation of agriculture is needed for the coordination of European and world agriculture, for the improvement of nutrition, and for the assistance to the depressed agricultural areas in Europe. The policy of self-sufficiency must be abandoned. A coordination of industrial reconstruction would be most helpful, especially with regard to the industrialization program of the retarded regions. The development of this part of Europe is a prerequisite to the economic and political consolidation of Europe. The formation of regional groups of small nations should be supported by all means if it could help in expanding production and trade and of course in promoting political stability.

CHAPTER TEN

THE PROBLEM OF GERMANY

GERMANY'S POSITION IN EUROPEAN TRADE

THE ECONOMIC DEVELOPMENT of the European Continent will be influenced by the changes in the position of Germany, which before the outbreak of the present war was the leading industrial power and the greatest trading country on the Continent.

Of the total imports of the European countries, Germany accounted for 24.5 per cent in 1928, for 20 per cent in 1935, and for 23.9 per cent in 1938. Her share of total exports was 25.1 per cent in 1928, 24 per cent in 1935, and 26.1 per cent in 1938. Her export was more than double that of France, totaling \$1,722 million in 1935 and \$2,117 million in 1938; the corresponding French figures for the same years were \$1,028 million and \$875 million. German imports amounted to \$1,677 million in 1935 and \$2,195 million in 1938; in the same years, French imports totaled \$1,392 million and \$1,326 million, respectively.

Germany's economic activity had repercussions in all European countries: a high level of employment in Germany spread to the rest of the Continent. Conversely, depression in Germany has always aggravated the economic troubles of all Europe. Such interrelation was natural and logical, especially before the rise of the Nazi regime; that is, as long as commercial relations between Germany and the Continent were on a more or less normal basis. It can perhaps be said that for a great number of European countries the importance of high business activity in

Germany was in normal times similar to the reaction in a large part of the world to a high level of employment in the United States.

In 1938 Germany disposed of 62 per cent of her export within continental Europe (nearly the same percentage as in 1928), and imported from it nearly half of her total import (43 per cent in 1928). Great Britain's share in Germany's export in the 1936-1938 period was 7.5 per cent and in her import, 5.6 per cent. The countries outside Europe bought 31 per cent of the total German export, supplying her with 46 per cent of her import. Germany accounted in 1928 for about a third of continental Europe's net imports from other continents. The deficit resulting from this trade was met to a large degree by her export surplus with Western and Northern Europe. During the thirties German exports were directed to a greater extent to countries exporting primary products—Latin America and Southeastern Europe—a development which made financing of the imports from these countries independent of the trade surplus with Western and Northern Europe. Germany's surplus balance with industrial Europe including Great Britain declined from \$550 million (at the devalued dollar level) in 1928 to only \$235 million in 1938. In the years before the second World War about two fifths of the German import consisted of foodstuffs and fodder including oilseeds; about 45 per cent were raw materials and semi-manufactured goods. German exports, higher in manufactured goods even than the British, were primarily designed for the industrial and generally highly developed countries of Western and Central Europe.¹ Germany had very diversified export industries: iron and steel products, tools, cutlery, machinery of all kinds, vehicles, represented about 45 per cent of

¹ See League of Nations, *Europe's Trade* (Geneva, 1941), pp. 41-42.

the total; chemical and pharmaceutical products followed with 15 per cent; textiles with nearly 10 per cent; coal and coke, nearly 10 per cent; paper, 3 per cent; glass and china, 3 per cent; instruments and watches, 10 per cent. This diversification, aided by a relatively large domestic market, together with a great flexibility in adjusting to new requirements, added to the strong competitive position of German products.

The importance of this trade to the European countries is clearly seen from the fact that it absorbed more than 10 per cent of the total trade of each country except France. The following series of figures indicate the position. During 1935-1937 imports from Germany amounted to 10 to 20 per cent of total imports of the following countries. (The figures in parentheses are for 1929.)

Belgium	11.7 (13.8)	Austria	16.5 (21)
Spain	13.4 (10.5)	Norway	16.8 (24.4)
Portugal	14 (15)	Czechoslovakia	17 (25)
Lithuania	14.1 (49)	Finland	19.5 (38.8)
Poland and Danzig	14.4 (27.3)		

From 20 to 30 per cent:

Sweden	23.8 (30.8)	Italy	27.2 (12.5)
Greece	23.8 (9.4)	Estonia	27.4 (30.1)
Switzerland	24.5 (25.1)	Hungary	28.2 (20)
Yugoslavia	25 (15.6)	Rumania	29.6 (24.1)
Netherlands	26.6 (30.6)		

Over 30 per cent:

Bulgaria 36.5 (22.2); Latvia 34.1 (41.2).

In regard to exports, during the same period Germany bought between 10 and 20 per cent of the total of the following countries (the figures in parentheses are for 1929):

Lithuania	10.3 (59.4)	Sweden	15.1 (15.2)
Belgium	10.4 (12)	Austria	15.5 (16.5)
Finland	10.8 (14.4)	Netherlands	16.7 (22.9)
Portugal	12 (17)	Italy	17 (11.9)
Spain	13 (7.4)	Rumania	17.6 (27.6)
Norway	13.1 (13)	Denmark	18.5 (19.9)
Czechoslovakia	14.6 (19.3)	Switzerland	18.6 (16.9)
Poland and Danzig	14.7 (31.2)		

From 20 to 30 per cent: Yugoslavia 21.3 (8.5); Estonia 26 (26.6); Latvia 32.8 (59.4).

Over 30 per cent: Hungary 30.2 (12.7); Greece 32.4 (23.2); Bulgaria 46.2 (29.9).

France exported 5.7 per cent of her total export to Germany (9.4 per cent in 1929) and imported from her 7.7 per cent (11.4 per cent in 1929). The figures for Great Britain were: export to Germany 4.3 per cent (5.1 in 1929), and imports from Germany 3.97 per cent (6 per cent in 1929).

The figures also indicate the shift in German trade toward the Danubian and Balkan countries, whose share in German imports increased from 4 per cent in 1928 to 12 per cent in 1938, and their share in German exports from 5 per cent in 1928 to 13 per cent in 1938; correspondingly, Germany accounted in 1938 for 34 per cent of the exports and for 35 per cent of the imports of the aggregate trade of Bulgaria, Greece, Hungary, Rumania, and Yugoslavia.

A quick perusal of the figures is sufficient to illustrate the importance of the trade relations with Germany for the majority of the European countries, both as buyer and as supplier of numerous goods. In spite of the very restrictive trade policy of Nazi Germany, she remained an important trading partner, even if we disregard her dominating position in trade with the agricultural countries in Southeastern Europe.

The war has obviously changed much of the structure of the German trade with the rest of Europe; yet it has not changed all fundamental conditions which had favored the development of this trade, such as central geographical position, good communications, technical efficiency and flexibility, and knowledge of the local markets.

ECONOMIC DISARMAMENT OF GERMANY

Peacetime Europe was naturally interested in Germany's prosperity because the increase in German purchasing power and her needs for import automatically spread to most of the other European countries. And as the development in the thirties has shown, it was difficult to find a new foreign market to replace the lost German market. Thus, if we consider the problem of Germany simply from the economic point of view, we must naturally conclude that German prosperity benefits all Europe. However, the experiences of the war and the history of the interwar period prove that we cannot at present confine ourselves to economic terms.

The problem in itself is not entirely new; it emerged in different form after the first World War. At that time French policy, in particular, was confronted with the dilemma either of obtaining large reparation payments, and to that end necessarily permitting Germany to make a quick recovery of economic and consequently also of political strength, or to keep her weak at the price of reducing the demand for reparations. The problem was not clearly seen, and the influx of foreign credits into Germany in the twenties concealed its true nature. Yet this time the whole problem is well understood and any decision should be based on full knowledge of the facts, circumstances, and the implications. We know the value of a prosperous peacetime

German economy for the rest of Europe, especially if, abandoning the policy of autarky, it reenters freer international trade. But we are equally aware of the danger inherent in German economic strength, particularly when coupled with an aggressive general policy. This danger becomes even more menacing if Germany is faced with a disrupted Europe and is surrounded by a number of small nations, some of which are economically weak.

A new dilemma will confront Europe in several instances, namely the choice between prosperity and security.² We may say that increasing prosperity will build a better base for a durable peace; yet a strong new Germany, basically unchanged in political and moral attitude, may well precipitate a new war. On the other hand, if for reasons of security Germany's economic strength should be greatly reduced, economic difficulties and political complications may ensue. There is general agreement that Germany must be economically disarmed, that her economic structure must be so changed that she will not possess the strength to start a new war. But there is a wide difference of opinion concerning the manner in which this objective can be attained.

It is not possible to define at present, even in approximate terms, the economic conditions of Germany; its entire production has been reorganized for war and its industries located for that purpose. Conversion to war production reached a higher level than in any other industrial country; some estimates have put present industrial production for civilian needs as low as 15 per cent of the whole output. Nobody knows, for instance,

² "What Kind of Peace with Germany" states that security takes priority over all other considerations in determining the small nations' various plans for the treatment of Germany. Winifred N. Hadsel, in *Foreign Policy Reports*, Nov., 1944, p. 211.

the exact volume of German production during 1943, and nobody can tell how large a part of the industrial capacity will be destroyed before the end of the war. The whole economy of the new Germany will have to be reorganized for peace. This task will begin during the occupation period, the length of which we do not know. It is highly desirable, however, that the United Nations have a common, concrete program for dealing with this problem. The report of the Crimea Conference of February 12, 1945, is not very definite on this point. It says in general terms, that "all German industry that could be used for military production" is to be eliminated or controlled, but does not specify what these industries are.

The question is, first, what kind of economic measures should be taken to make a new aggression economically impossible or extremely difficult. A recent study published by the Brookings Institution examines a number of economic measures ³ and emphasizes the impracticability of economic plans designed to destroy once and for all the industrialism on which war power rests. The reduction of a highly developed industrial country to an agricultural status would leave a vast population incapable of supporting itself, and would disorganize and contract international trade at the very time when expansion of world trade is most needed. The authors recommend some specific measures, in particular the suppression of aluminum ingot production, the prohibition of synthetic oil plants, prohibition of commercial as well as military aviation, control to the greatest possible extent of electric power production and consumption in

³ Harold G. Moulton and Louis Marlio, *The Control of Germany and Japan* (Washington, D.C., 1944). See also H. N. Brailsford, *Our Settlement with Germany* (New York, 1944), pp. 109 ff.; and the Royal Institute of International Affairs, *The Problem of Germany* (London, 1943), p. 41; Sir Walter Layton, *How to Deal with Germany* (London, 1944), p. 49; "Terms for Germany," *Economist*, Aug. 12, 1944.

Germany, making Germany dependent on a supply of electric power from foreign countries—France, Belgium, Norway, Italy, and Austria. All these suggested economic measures would be “a useful adjunct to armament reduction and military control.” The whole scheme is well conceived. It attempts to weaken the German economic war potential in a few key items that will not interfere with the German economy in general, and to avoid the undesirable repercussions on other countries, especially in Europe,⁴ of a greatly weakened German economic structure. We certainly agree with the conclusion that no plan can prevent Germany from preparing for war unless coupled with military control backed by a united front of the major powers. Though the main idea seems correct, the economic disarmament of Germany has to go farther than is suggested in the Brookings study. It must not be forgotten that the whole trend of the German economy since 1933 has to be reversed and the Nazis’ New Order annulled. Because the armed economy was introduced during peacetime, reconversion there has a different aspect than in Great Britain and the United States where war production started during the war.

A program of economic disarmament, of reconversion to peace must also aim at a reintegration of the German economy into European and world economy. In the field of agriculture such a program means the abandonment of the policy of high protection which in the thirties took the clear form of self-sufficiency. As we explained in the previous chapter, this change will bring about a shift from high-cost grain production to an expanded production of protective foods. It will increase Ger-

⁴ In the Royal Institute, *The Problem of Germany*, p. 42, we find the statement that “Deliberately to ruin German productive capacity, both industrial and scientific, would involve the further depression of the standards of living of other European countries.”

many's import of bread cereals and fodder from Eastern Europe and overseas; Germany's dependency on grain imports will increase, and thus by itself put a certain brake on military adventures. The period of occupation is well suited for starting this program and organizing its execution. The plan assumes that the long-delayed land reform will be carried out, and the large estates owned by the Junkers will be split up. The land reform, while strengthening the position of the small farmers and peasant owners, will destroy the economic backbone of the political power of the Junkers. The trend in German agricultural and commercial policy, which began in 1879, will thus be reversed.

Industrial disarmament in a broad sense should consist in eliminating from German industry the new or expanded capacity which was added during the Nazi regime in order to prepare for war and, particularly, to counteract blockade. So the high-cost substitute (*Ersatz*) production of synthetic oil, rubber, and even some textile fibers (like those used as wool substitutes) should be suppressed; the same should apply to the mining of high-cost low-grade ores of iron, copper, and tin. The production of aluminum, by means of imported bauxite and coal-generated electric power, is also a high-cost production, and could be profitably moved for instance to Yugoslavia, where better conditions for production are found. In a number of industries the production capacity for military purposes ⁵ should be reduced.

Germany's productive capacity in iron and steel, ferro-alloys, metallurgical engineering, and chemicals had been so exten-

⁵ In 1938, Germany produced more than 55 per cent of the continental steel production, more than 55 per cent of the aluminum production, two fifths of cement, 40 per cent of rayon, more than half of the artificial fibers, 25 per cent of wood pulp, and more than one third of the European production of sulphuric acid.

sively increased before and during the war that to leave it in its present state, even if the expected destruction is taken into account, would still give her too great strength. The destruction resulting from war is seldom so thorough as to make reconstruction very difficult. German capacity in the leading industries in 1933 should be taken as a basis which, except for technological reasons, should not be surpassed. The execution of these directives would automatically help to fulfill economic disarmament in the narrow sense, namely the elimination of all factories producing armament of any sort, including ammunition and explosives. In connection with this problem the synthetic nitrogen industry should be examined. This industry has been greatly expanded not only in Germany but throughout the world. If oil is considered indispensable for war, the same should apply to nitrogen. The removal of the synthetic nitrogen industry from Germany would not paralyze even the German chemical industry. Nitrogen fertilizers, which will be easily available, and nitrogen for the chemical industry (for instance, in the manufacturing of the dyestuffs) can be imported. After all, the highly developed Swiss dyestuffs industry has for a long time imported the basic inorganic chemicals. It is only a problem of the balance of trade, not more difficult than in the case of rubber or oil.

In place of the proposed reduction of the German industrial potential, a long-term United Nations control of German industries as an adequate security measure was suggested. One such plan, advanced by the Dutch, proposed to maintain a strict supervision over German industries by controlling the majority of stock in these plants.⁶ Majority shares of stock in German industry should be computed by each nation on the basis of repara-

⁶ Winifred N. Hadsel, "What Kind of Peace with Germany," *Foreign Policy Reports*, Nov. 15, 1944, p. 217.

tion claims against Germany and be placed in the trusteeship of an international agency. The author of this plan holds that control of means of production will be more effective in preventing rearmament than measures designed to destroy Germany's industrial potential. There is certainly much to be said for the argument. Yet the liberated nations will want to have a more tangible guarantee than mere control of shares; the removal of a strategically important part of the German industrial machinery will be of greater reassurance to them than control of a few factories located in Germany.

There remains the question of the German cartels and trusts. The danger of the cartels has often been exaggerated. Once the German domination of Europe is overthrown, German industrial holdings in European countries seized, German patents made available to the United Nations, it will not be difficult to disentangle any cartel ties and to reorganize national industries. The problem of trusts or combines is a more complicated matter. It would not be economically advantageous to dissolve units such as vertically concentrated plants brought together for technological reasons. Yet there are several trusts in Germany which grew in dimensions far beyond any technological justification. There is no need to supply special proofs that the Hermann Goering Werke are not an organically composed and technologically interrelated enterprise. Even the I. G. Farben, in spite of all arguments favoring concentration in the chemical industry, should be divided into several units, each of which would represent a well-rounded chemical concern with a sound technical basis. The same can be said in regard to several iron and steel concerns.

If the whole program—agricultural as well as industrial—is

carried out, it could bring about the economic disarmament of Germany; change her economic structure; and make possible her economic integration with the European and world economy. Though removing a perhaps substantial part of the German economic strength as a safety margin, it does not entail the deindustrialization of Germany, although it does require a change in industrial structure. From several sides it has been proposed that Germany should concentrate on consumer goods industries like textiles, leather and shoes, toys, glass and china. In view of the structure of the German export and also of the trend of industrialization throughout the world, it can hardly be presumed that a limitation to consumer goods industries would provide enough export and employment.

THE REPARATIONS PROBLEM

Germany's economic importance will automatically be diminished as a result of a lost and costly war. Obviously, the United Nations will first take care of the relief and reconstruction of the countries which were victimized by Germany. A Germany impoverished by the war, with productive machinery in great part destroyed, with no foreign exchange (the amounts she possesses she will have to return to the countries despoiled and occupied), and with a completely unbalanced social structure, cannot be a strong buyer of foreign goods. During the first years after the war, the European producers of agricultural as well as of industrial commodities will probably have no difficulties in finding markets for their goods. At any rate, they will not be anxious to enter into trade relations with Germany; in many European countries the people will probably refuse to buy German products. During this period new trade channels can

be tried out and organized to replace the German market as far as it will prove necessary.⁷

Another important problem affecting the German economic position is the payment of reparations and indemnity. It is not a matter of controversy that the Germans must restore the loot taken from the occupied countries, or give equivalent goods if the originals have been lost, destroyed, or consumed; neither is there any doubt that all German property outside Germany, including patents, will be seized in favor of the United Nations. The list of claims against Germany is in itself very long; and if, as a basis for reparations, we begin to count all the damages done by the actual warfare, we shall arrive at extremely high figures. Yet we have learned our lesson from the experiences made with the reparations problem after the last war. It is evident that if Germany is to pay large reparations, her productive machinery must be restored and made efficient (which might not be in agreement with the plan for Germany's economic disarmament). And, generally speaking, the statement made with regard to the German reparation by John H. Williams in 1932, namely, that "large, arbitrary payments of this sort are bound to distort the international economic structure"⁸ is still true.

Based on previous experience with German reparations, the opinion now prevails that payments should be demanded not

⁷ "What Kind of Peace with Germany," *Foreign Policy Reports*, Nov. 15, 1944, p. 217, in discussing deindustrialization of Germany, points out that the French, Belgians, Czechs, and other Europeans who have their own raw materials and skilled labor would be glad to eliminate German competition in the field of heavy industries and increase their own development along this line. On the other hand, however, there are European nations who have important agricultural exports and are used to selling large quantities of their produce in the German market. This is true of the Netherlands, Denmark, the Danubian and the Balkan countries. These nations would not like to lose the German market for their products.

⁸ John H. Williams, *Postwar Monetary Plans* (New York, 1944), p. 168.

in foreign exchange but either directly in kind or in German currency, to be used for purchases of German goods within a definite time limit. Any kind of payment presumes the debtor's ability to produce the demanded goods and to deliver them without obtaining as countervalue any goods from abroad. Germany's industrial achievements before and during the war leave no doubt of her ability to produce and deliver a large amount of goods without reducing the level of living. Even a part of that portion of national production which before the war was devoted to armament would represent sizable reparations. This whole problem is, of course, related to the question of how strong German industry should be allowed to be.

The other aspect of reparation payments is the willingness of the creditors to receive deliveries from abroad without exporting their own goods and services as payment for them. The experience after the first World War has shown that the reparations-receiving countries, though they wanted the payments, were opposed to having their export affected by the consequences of reparations on international trade. This time there may be one decisive difference. Whereas the creditors of the German reparations were mostly countries with highly developed industries and with import surplus and capital export, now the most intensive demand for reparations will probably come from the Soviet Union, Poland, Yugoslavia, and Greece. It might be more feasible to arrange reparations in kind for them. Russia will need a large amount of all kinds of capital goods—locomotives, generators, tools, and machinery—and also many consumer goods. Thus, reparation payments would perform a role similar to foreign loans used for buying such imports. In the other countries mentioned above, the situation will be very similar. They will all need capital imports, and this need could,

to a certain degree, be satisfied by the German reparation deliveries, which will also play a role in the program for economic development of the backward areas. Industrial machinery, railroad rolling stock, and livestock could be shipped to these countries within a short period either as reparation payments or restitution of looted or destroyed goods. The transfer of industrial equipment made available by the economic disarmament of Germany also falls in this category.

A possible objection that getting imports from Germany as reparation payments will make it difficult for the receiving countries to export their goods to Germany could be met by the argument that during the first years after the war these countries will have no great difficulty in selling their goods, and, furthermore, that they will not need to export all of them if they are able to get the required imports without payment. This point is particularly clear in the case of the Soviet Union. She can point out that her need for goods from abroad will be much greater than her need to find markets for her export. Therefore, she will not lose any outlet by receiving large reparation deliveries from Germany.

Nevertheless, the following problems should be considered: First, countries not receiving reparations might feel that Germany's capacity to buy their goods is being impaired by continuous large reparations; second, substantial reparations would require that the German capital goods industry be rebuilt in a shorter time and on a larger scale than would be desirable for reasons of security. Furthermore, Germany will need imports of raw materials and food in order to be able to produce the demanded goods.

A reparations program should be worked out and agreed upon

among the United Nations within the shortest possible time. All implications should be taken into account. The duration of the payments should be fixed in advance and should not exceed a period of ten years. As soon as an agreement among the United Nations is reached it should immediately be made public. It should include the total duration of the payments and the amounts and quantities which will be received by the respective countries. Professor J. Viner is certainly right in demanding that no country should be permitted any claim for reparations beyond an amount of goods which the country guarantees it can absorb without disturbing its normal trade relations with Germany and with other countries.⁹

The goods to be delivered as reparation payments should preferably be products to which the German war industry can best be converted. Economic disarmament and reparations deliveries should be closely related and both should be adjusted to a general program of reconstruction. The period of transition and of transformation of the German economy will be the one best suited for reparations deliveries which, on the other hand, will perform the role of capital imports in some of the receiving countries. And it can be assumed that during this period these countries will not depend on the German market for their export.

The Crimean Conference in dealing with the reparations problem stated in general terms that it recognized as "just that Germany be obliged to make compensation" for the damage caused by her to the Allied Nations "in kind to the greatest extent possible." The Conference agreed to establish a commission to consider the question of the extent and methods of

⁹ Jacob Viner, "German Reparations Once More," *Foreign Affairs* (1943), p. 673.

compensation for this damage. The commission should be able to work out a solution that will be well balanced economically and politically.

TRANSFORMATION OF THE GERMAN ECONOMY

Everyone realizes that Germany's economic position in Europe and the structure of her economy must and will be changed. The effects of the war itself will cause a great reduction in the level of living and in buying power; economic disarmament will produce further substantial changes. Germany will cease to be a big power.

The great bulk of transformation of the German economy should be accomplished during the occupation period under the guidance of the occupation authorities. The United Nations are powerful enough to do with the German economy whatever they consider necessary and useful and the German people should be made to understand this. It can be calculated in advance in broad terms what the effects of the planned transformation of the German economy on the economy of other countries will be, and measures can be taken to offset unfavorable consequences. As a matter of fact, when determining an economic program which considers the problem of security as related to prosperity, the leading powers will need to have a thorough analysis of the expected consequences of such developments, particularly on the European Continent.¹⁰ And a plan will have to be prepared to take care of any unfavorable situation that may arise for some one country. It would be unfortunate indeed if

¹⁰ Sir Walter Layton (*How to Deal with Germany*, p. 49) states with emphasis that it is impossible to legislate for the economic future of Germany or divide up the mineral resources near its borders without regard to the future economy of Europe as a whole. Any project for dealing economically with Germany must be part of this greater whole.

the events of the economic sanctions against Italy in 1935 should be repeated under changed circumstances. At that time, the small nations, loyally carrying out the sanctions and losing their export to Italy, expected economic assistance which had been promised by the big powers but never materialized.

It is not within the province of this study to analyze the economic effects of territorial changes often proposed at present, as the formation under international sovereignty of a large bridgehead (the Rhine-Ruhr industrial area) or the cessation to Poland of a part of East Prussia west and south of Königsberg and other parts of the territory east of the Oder, accompanied by a transfer of populations.¹¹ In dealing with the eastern frontier of Poland at the Crimean Conference, the big three considered that this should follow the Curzon Line (with digressions from it in some regions of five to eight kilometers in favor of Poland), and they recognized that Poland must receive substantial accessions of territory in the north and west. The final determination of the western frontier of Poland, that is, of the eastern border of Germany should, however, await the peace conference. The United Nations will have the power to impose

¹¹ Analyzing these plans, *The Economist* of Oct. 7, 1944, p. 478, in an article, "Between Rhine and Oder," points out that if these two changes were to take place and the contemplated transfer of German population including 3½ million Germans from Czechoslovakia were carried out, then Germany as it was before the Anschluss of Austria, would lose roughly one third of its territory but only 16 per cent of its population. *The Economist's* opinion is that this new Germany could not exist as a self-supporting unit and even that Germany might then become a place of mass unemployment, mass undernourishment, and perpetual political tension.

Foreign Policy Reports, "What Kind of Peace With Germany" (p. 214) calculates that if all territorial changes proposed by the French, Dutch and the rival Polish groups were carried into effect, Germany would lose approximately one fifth of the pre-1938 area. Germany's coal and steel production would be reduced by these cessions by one fourth, compared with the prewar output; important zinc, lead, and lignite revenues would also be lost.

any settlement upon which they agree, and they will be able to carry it out. However, the effects of all such changes on Europe, on the country into which a part of Germany is incorporated, and on the situation of Germany itself would have to be appraised in all their ramifications. It will be necessary to determine what further readjustments are necessary. Nevertheless, whatever these changes and readjustments may be, the points we have made in regard to the economic problems of Germany (whose area is here understood as it was before the occupation of Austria) remain pertinent.

The German economy must be reconstructed for the peace not only of Europe but of the world. However, any substantial alteration will have repercussions on the national economies of the other European nations. *The big economic powers will definitely have to help the Continent of Europe to bear the task of any adjustment resulting from the transformation of the German economy.* There will be no great problem in replacing German exports. And, as can be anticipated, some countries—Great Britain and the United States among them—hope to take over the markets which the German industry lost not only in Europe but also in Latin America and elsewhere. There is no doubt that it is possible to replace practically all German industrial products. This, however, is only part of the problem. Countries that expect to take Germany's place in supplying goods must be willing also to take its place in buying goods. For many of the countries this side of the problem will not be so easily solved.¹² The figures of German trade with the European coun-

¹² In the *Problem of Germany*, p. 42, it is stated that even British employment would suffer to some extent from the impoverishment of Germany as a customer; and that it is doubtful if this loss would be offset by her elimination as an export competitor. (Great Britain exported in the thirties to Germany only 4.3 per cent of her total exports.)

tries indicate clearly enough the interrelation between import from and export to Germany; they show the complicated intricacy of the problem of shifting sources of supply and outlets for exports.

If, as a result of the war, of the needed transformation of her economy, and of economic disarmament, the German's standard of living is lower for a number of years, she will not be able to buy many of the goods normally imported from European and non-European countries. Not all countries will feel that loss with the same intensity.¹³ The most severely hit will probably be the economically weaker states of Central and South-eastern Europe, especially those dependent on Germany as a market for their staple products. Therefore, there should be a sustained endeavor to improve the position of these countries, whose economical and political importance to Europe has been demonstrated by the German penetration. During the period of transformation of the German economy every effort should be made to accelerate the economic growth of the backward areas even with the aid of transferred German equipment or plants. An increased economic strength and political as well as economic agreements will eventually make this part of Europe stronger against any possible new aggression. The major powers, including Western Europe as well as the Soviet Union, should meet a future German menace with a strong and sustained co-operation with these nations. Thus confronted, Germany's position would not be even relatively strong, because the strength of the economically weak nations would have increased. Co-operation of this sort is the logical road to a new economic or-

¹³ It is well remembered how few goods the Western powers bought from Southeastern Europe in the thirties, although such purchases were the main instrument in weakening the German ascendancy there.

ganization of Europe with Germany again as a useful partner.¹⁴

The economic disarmament of Germany will be carried out during the period of occupation or control; and at the same time the economic transformation of Germany will have to be performed. During this period her political reconstruction will proceed. When the chief consequences of her armed economy have been eliminated, Germany may be ready to participate in a new European economy, in which substantial progress has been made toward the goal of more equal standards of living in Europe as a whole. Our objective should be not to keep Germany isolated and controlled for an indefinite period but to bring a reshaped German economy back into genuine cooperation with the rest of the world, assuming that a new Germany will prove worthy of trust and of admission into the family of nations.

¹⁴ See the specific proposals in Sir Walter Layton's *How to Deal with Germany*; also, "Industrializing the 'Lebensraum,'" *Financial News*, Sept. 23, 1944.

CHAPTER ELEVEN

TRADE WITH THE SOVIET UNION

THE SOVIET UNION will emerge from this war as one of the most important world powers. She has returned to world politics demanding, and willing to assume, the role appropriate to her position. Wielding great weight in politics, she could and should become an equally influential factor in world economy.

The economic development of the world, but especially of continental Europe, was undoubtedly affected by the Russian situation during the interwar period. Whereas Russian industrial production rapidly increased in the thirties and has reached a level several times higher than before 1914, her share in world trade, which was low even before the first World War, has greatly declined. Over the period of 1925–1937 both Russian export and import amounted roughly to 1.5 per cent of world exports and imports. (In 1938 the import was only 1.1 per cent and the export 1.25 per cent of the world's total.) In no year after the war has Russian foreign trade reached the volume of 1913, when imports were 3.6 per cent of world imports and exports 4.2 per cent of the world total.¹ Even at that time Russia's

¹ The figures for the Russian foreign trade (in value as well as in weight) clearly show that during the whole interwar period the Russian postwar trade did not reach the prewar level. Exports in 1913 amounted to 1,520 million rubles, in 1936 to 367.4 million rubles; the highest amount was reached in 1930 with 1,036 million rubles. The weight figures are (in thousand tons): 24.113 in 1913, 12.969 in 1938; the highest was 21.779 in 1931. The development in imports was similar: 1,375 million rubles in 1913, 242 million rubles in 1936, the highest amount 1,105 million rubles in 1931; and against 15,343,000 tons in 1913,

trade compared unfavorably with that of all other large European countries, and in the thirties it fell below the level of the twenties. In 1937 imports, as computed by Russian sources, were just about one fifth those of 1931. The reasons for this development are too well known to need special discussion here. The whole foreign trade was carried on as a government monopoly, and was planned down to the minutest details; the plan was adjusted to a general economic program oriented towards autarky.

Though Russian trade before the outbreak of the second World War is not a good basis for any calculation of postwar possibilities, a few figures illustrate the relation to the entire European trade. In 1938, exports totaled \$257 million; in 1935, \$326 million; and in 1928, \$413 million. Imports were \$268 million in 1938; \$210 million in 1935; and \$491 million in 1928. Russia's foreign trade in the thirties was in fact smaller than that of Switzerland and Czechoslovakia, and about one third that of Canada. In 1938 Russia sent to continental Europe 46 per cent of her total export (54 per cent in 1928), to Great Britain 30 per cent (20 per cent in 1928)—or to Europe in general 76 per cent (74 per cent in 1928)—and to the United States 8 per cent (6 per cent in 1928).² In 1938 Russia imported from continental Europe 30 per cent of her total imports (40 per cent in 1928), from Great Britain 11 per cent (only 20 per cent in 1928), and from the United States 30 per cent (19 per cent in 1928). Twenty-five years earlier (in 1913) Russia had sold to Europe about 90 per cent of her exports (Central Europe accounting for 52 per cent) and had bought from Europe nearly

only 1,285,000 tons in 1938, with 3,564,000 being the highest volume in 1931. S. P. Turin, *The U.S.S.R., an Economic and Social Survey* (London, 1944).

² League of Nations, *The Network of World Trade* (Geneva, 1943), p. 65.

80 per cent of her total imports (about 52 per cent from Central Europe).

During the thirties, there was an export surplus with Western Europe and the Scandinavian countries; this was needed to meet the import deficit, especially with the United States and the British Dominions. So, for example, in 1935 Russia's export surplus with industrial continental Europe was \$47 million (\$13 million in 1938), with Great Britain, \$42 million (\$29 million in 1938); with other than industrial countries in Europe, \$18 million (\$16 million in 1938). Thus in 1935 the total export surplus with Europe was \$107 million, against an export surplus of \$58 million in 1938.³

Under the Nazi regime, Russia's trade with Germany was substantially reduced; her imports from that country declined from 25 per cent of the total imports in 1928 to only 4 per cent in 1938, while her exports dropped from 24 to 8 per cent in the same period. But, in spite of this reduced trade with Germany, continental Europe supplied in 1938 nearly one third of the imports and bought nearly one half of the exports of Russia in the last prewar years. Conversely in 1928 and 1938, European exports to Russia amounted to only a little over 2 per cent of the export from the European Continent (compared with 35 per cent of the total from the Continent to Great Britain) and imports from Russia equaled in 1938 less than 2 per cent of the total imports of continental Europe from the rest of the world (less than 4 per cent in 1928). Continental Europe in 1938 carried on a greater trade with Australia and New Zealand

³ According to Russian statistics the export surplus with Europe totaled in 1937 532.5 million rubles, with Western Europe 587.7 million rubles. The import deficit with the American Continent and the British Dominions was 207.5 million rubles. Alexander Gerschenkron, *Economic Relations with the U.S.S.R.* (New York, 1945), p. 33.

combined than with Russia. "Russia has ceased to be the granary of Europe and has lost the attraction as a big European market."⁴

Obviously, the Russian share in trade with single European countries was also very small. During the period of 1935–1937 only four countries (the Baltic states not included) exported to Russia more than 1 per cent of their total exports (1929 figures in parentheses): Germany, 2.8 (2.6); the Netherlands, 1.9 (0.1); Belgium 1.5 (0.3); and Czechoslovakia 1.4 (1.3). The figure for Great Britain was 0.7 (0.5). In turn, Russia provided only four countries (again the Baltic states are not included)⁵ with more than 2 per cent of their total imports: Belgium 3 (0.6); Greece 2.9 (2.1); Germany 2.8 (3.2); and the Netherlands 2.4 (1.5). Of the British imports her contribution was 2.1 per cent. Czechoslovakia, Denmark, Finland, France, Norway, Poland, and Sweden imported from Russia between 1 and 2 per cent of their total imports. The trade with the Soviet Union represented less than half of one per cent of the total trade of the Danubian agricultural countries—Hungary, Rumania, Yugoslavia, and Bulgaria—which were all subjected to the German economic penetration.

The structure of the Russian foreign trade was rather simple. In 1937, 12 per cent of the imports consisted of foodstuffs and live animals; 50 per cent, materials, raw or partly manufactured; and 38 per cent, manufactured articles.

⁴ Turin, *The U.S.S.R.*, p. 153.

⁵ During this period the trade of the Soviet Union with the three Baltic States in percentage of their total trade (1929 figures in parentheses) is shown by the following figures:

	<i>Export to Russia</i>	<i>Import from Russia</i>
Estonia	3.4(2.4)	5 (4.2)
Latvia	2.8(14.6)	3.5(4.7)
Lithuania	6.4(0.4)	5.1(6.3)

The lack of foreign exchange induced Russia to limit her import considerably; the decision to industrialize the country according to successive five-year plans implied that those imports should have priority which served the industrial production. The plans gave priority to imports of capital goods and of raw materials and kept at a very low level the imports of goods for consumption and even of raw materials needed for the production of consumer goods.⁶ Machinery of all kinds held first place, with 23 per cent of the total (1935–1937 average); metals and crude semimanufactures came to 17 per cent; iron and steel manufactures to 8 per cent; wool, 5.8 per cent; rubber, 5.4 per cent; cotton, 4 per cent; tea, 2.2 per cent. Consumer goods amounted to 12 per cent.

The structure of the Russian export may be seen from the following figures for the year 1938: foodstuffs and live animals, 24 per cent (1933–1937 averages are 18 per cent); materials, raw and partly manufactured, 58 per cent (1933–1937, 61 per cent); manufactured articles, 18 per cent (1933–1937, 21 per cent). In 1913 agricultural products accounted for 73.8 per cent and industrial products for 26.2 per cent.

During the period 1935–1937 timber and manufactured wood accounted for 25.5 per cent of the total exports (Great Britain bought 40 per cent of the total timber exports), crude petroleum and petroleum products for 11 per cent; grain for 8.5 per cent; undressed fur skins for 6 per cent; flax for 4.6 per cent; manganese ore for 2 per cent; various foodstuffs, 9 per cent; coal, 2.5 per cent; cotton piece goods, 4.4 per cent (exported mainly

⁶ Imports for consumption in 1933–37 were in absolute value about one tenth those of 1909–13, in relation to total imports they were more than halved. S. N. Bakulin and D. D. Mishustin, comp., *Vneshniaia torgovlia S.S.S.R. za liet, 1918–37* [twenty years of Foreign Trade of the U.S.S.R.] (Moscow, 1939), p. 16; quoted by Gerschenkron, *op. cit.*, p. 57.

to the neighboring areas in Asia). The value of exports in 1936 amounted to only 0.8 per cent of the gross production of the U.S.S.R. and the average in the period of 1933–1936 was 1.5 per cent.⁷

Looking at the figures of the Russian foreign trade in the interwar period, one is inclined to speculate what a different turn the development of Europe might have taken if Russia had participated more actively in economic cooperation with the rest of the world. What advantage could Europe, and at the same time Russia herself, have gained if Russian foreign trade had kept pace even to a small degree with the expansion of domestic economy? There is a logical lesson here for the post-war world; namely, that the utmost should be done to establish durable and extensive economic relations with Russia, to bring her back to a working cooperation with an expanding world economy, and to convince her that such policy would also be to her own great advantage.

It is difficult to attempt a prediction concerning Russia's post-war trade. But in a country with Russia's resources, the existing and potential productive capacity would offer enormous scope for foreign trade. We know that the system of foreign trade monopoly will be maintained; it is a part of Russia's economic system. This, however, does not need to be a fundamental obstacle. Everything depends on the trend of the Russian foreign trade policy after the war. Will she continue to aim primarily at achieving self-sufficiency or will she be willing to join the rest of the world in a policy of mutual cooperation toward trade expansion and a more equitable division of international production? We do not as yet know the answer to this question.

⁷ D. D. Mishustin, ed., *Vneshniaia torgovlia S.S.S.R.* [Foreign Trade of the U.S.S.R.] (Moscow, 1941), p. 38; quoted by Gerschenkron, *op. cit.*, p. 55.

Nevertheless, there is growing evidence that the Soviet Union intends to take an active part in economic collaboration. She is a member of the United Nations Relief and Rehabilitation Administration, she participated at the United Nations Monetary Conference in Bretton Woods, and she is in favor of the International Security Organization which is supposed to set up an economic and social council vested with important functions. The feeling of political security, the removal of the danger of a new war, might have important bearing on her economic policy. It is evident even now that she will make every effort to rebuild her devastated areas quickly, to reconstruct her economy, and to continue in the general direction of her prewar economic policy. She will further increase her industrial capacity, exploit her resources, and expand productive capacity in many places where production had been established or enlarged during the war. That she will continue to build capital goods industries appears to be a foregone conclusion. Yet we have good reason to anticipate that the Russian people, who have been through the ordeal of this terrible war and who for a number of years have undergone drastic privations in order to achieve the industrial program, will now rightly demand an improvement in their standard of living. This would mean a greater supply of consumer goods and may have some influence on the government's policy regarding the import of such goods, and this not only during the first years after the war.

It is certainly an enormous task to rebuild the devastated areas, to put destroyed factories, public utilities and transport facilities back to work, and to replenish stocks of raw materials, agricultural machinery, and livestock. If Russia plans to speed up this reconstruction work, she will need to import capital goods in great quantities, as well as many other commodities

that would bring relief to the population and help to rehabilitate those areas which suffered most from enemy occupation. But the problem will again arise of how to pay for the necessary imports. It will probably take some time before exports can be organized even on a prewar low level. And the value of this prewar export will, of course, be entirely inadequate to meet the actual import requirements. The Soviet Union has not published figures concerning her gold reserves so that it is not known to what extent these could be used to pay for import deficits.⁸

Russia is certainly counting on reparations to offset part of the reconstruction costs. By the terms of the armistice closing the war with Finland and Rumania, in the course of the next six years each of those countries must pay \$300 million (an amount higher than the Russian export of 1938). These reparations are to be paid in kind. Rumania will deliver oil products, grain, timber, sea and river ships, various machine equipment, and similar items; Finland will furnish timber, paper, cellulose, sea and river ships, and various machine equipment. Some of these—oil products, grain, and timber—have figured among the chief articles of Russian export. From these facts we can get perhaps an idea of Russian needs after the war. Hungary, too, must pay reparations of \$300 million in kind—in agricultural products and machine equipment. Russia will receive \$200 million; Czechoslovakia and Yugoslavia, \$50 million each. These armistice terms also furnish some indication of the amount of reparations in kind which Russia may demand from Germany.

In addition to the expected reparations, Russia intends to accelerate her reconstruction through the use of large long-

⁸ The national gold reserve in 1936 was estimated at 33,000,000 fine ounces, or \$1,155 million. Turin, *op. cit.*, p. 63a.

term foreign credits. The United States is practically the only country able to grant long-term credits for such purposes, and the needed amounts are large indeed. If the credits were not limited to purchases in the United States, they would be of significant value for all countries able to deliver the goods required by Russia, and the United States would suffer no disadvantage, as the money would come back to her through purchases made by the other countries. Such a liberal lending policy would definitely support the case of multilateral trade. The effects would be similar if some countries were to obtain credits in order to finance their deliveries to Russia. One fact of primary importance should not be overlooked. Any credit granted to Russia will stimulate world trade. Large credits to be spent on United States deliveries would help to keep employment high in the United States and would have a favorable effect on imports. Similar consequences should follow in Russia. With production increased and improved, she should be able to export more diversified goods in greater quantities and, at the same time, to buy more goods from abroad. The Russian foreign trade policy should not stand in the way of the development usually following such international loans.

It is certain that a number of countries, particularly in Europe, look to Russia as a new great trading nation able to offset some of the lost export markets. From the structure of the Russian foreign trade, which will scarcely change as quickly as some experts think, it follows that her trade with the advanced industrial countries in Europe will have a different pattern from her trade with the agricultural countries in Eastern and South-eastern Europe. As soon as their machinery is put back to work, the industrial countries of Europe will probably be able to supply Russia with many of the needed capital goods and other

industrial products. Czechoslovakia, Belgium, France, Switzerland, Sweden, or Austria, and certainly Great Britain, can produce all kinds of machinery, tools, electrotechnical equipment, chemicals, and many semimanufactured products which Russia will need. Russia could continue selling to them the same type of goods as before the war, and she could expand this export as her production increases and improves.⁹

Russia will have to import a great deal more than she can export. It may be possible to pay for the import deficit in gold, as the yearly gold production is estimated to be \$150–200 million. It is problematical whether Western Europe will be able to maintain the deficit in trade with Russia that was used by Russia to meet her import surplus with the United States. At any rate, it cannot be doubted that trade possibilities between the Soviet Union and the industrial nations of Europe can expand much beyond the prewar level.

Russian trade with Eastern and Southeastern Europe presents another facet of the problem. What products could Russia buy, and what could she supply in turn? In normal times Russia can hardly be considered a regular buyer of the agricultural staple products exported by these countries. This is certainly true of wheat, barley, and rye—all grains which Russia herself exported;¹⁰ and applies equally to timber, fruit, fish, vegetables, lard and hogs (imports of livestock were very small). It remains to be seen whether Russia will become an importer of agricultural staple products as some experts anticipate, and, if so, how soon it will occur. This development is expected in the course of the rapid industrialization of Russia and of the predicted growth

⁹ Besides a number of agricultural products, those goods were timber, oil, fur, skins, flax and hemp, asbestos, manganese ore, and phosphates.

¹⁰ Before the war, Russia produced 50 per cent of the world production of rye, 20 per cent of wheat, 16 per cent of barley, and 20 per cent of oats.

of population together with the rising standard of living. Yet it should not be forgotten that Russia has great possibilities to increase the intensity of agricultural production and to enlarge greatly the cultivated area. While a general rise in the level of living will give an impetus to the import of tropical products and other specialized food articles, it would be premature to assume that it will create an import need of foodstuffs in general. Russia might perhaps use Balkan tobacco and a number of agricultural specialties; she may need some minerals as antimony, chromium ores, and even lead and zinc; and she may also be able to use some industrial products. During the period of transition, of course, Russia will offer a good market for almost all goods exported from these countries, and she might thus replace Germany as a buyer. Moreover, if trade between Russia and Western and Central Europe expands, the other European countries could increase their purchases in Eastern and Southeastern Europe.

The agricultural countries will not need many of the primary products exported by Russia, but they may well constitute a market for some manufactured goods. During the last years before the war, Russia exported some manufactured products though only in small quantities and chiefly to the neighboring parts of Asia.¹¹ As a result of reconversion and development of the Russian industry, numerous new products will certainly be added to those previously exported. As before 1913 Russia may again be in a position to export more goods to these countries than she can buy there.¹² She may also be able and willing to grant them some credits for their own economic development.

¹¹ Among these goods were tractors and various agricultural machinery, sewing machines, cement, and textiles.

¹² In 1913 Russia exported to the Balkan countries goods for 285 million and imported for only 92 million rubles (rubles equivalent to 1936 rubles).

Certainly, the Russian economy will be strong enough to establish regular trade relations with this retarded area of Europe, and although the prospects for trade here are at first not as favorable as with the industrial countries, the prewar volume was so small that there is room for considerable growth. The whole question hinges on the attitude of the Soviet government toward economic relations with these countries. The system of government trade monopoly together with the over-all planned Russian economy will enable Russia, for instance, to purchase even the surplus of agricultural staples, the amount of which will be small in comparison with the total consumption and production in Russia.

While the potentialities of an expansion of Europe's trade with Russia are great indeed, some important problems have to be clarified. Continental Europe is extremely interested in an expanded, assured, and regular trade with the Soviet Union on a scale which would greatly surpass the prewar level. Russian trade of the interwar period was erratic. Placing it on a multilateral basis would be generally beneficial, in view of the different trade possibilities between Russia and industrial Europe, Russia and agricultural Europe, and between the various parts of the Continent. The European nations would welcome a system providing for equality in trading opportunities. When small nations deal with big powers, they are always better off if they enjoy the most-favored-nation treatment. The manner in which the Russian trade monopoly was operated before the war made it necessary to supplement the most-favored-nation clause by elaborate provisions guaranteeing in fact an equality of trading opportunities. In the general interest, there should be a tendency to avoid such bilateral arrangements whereby Russia would undertake bulk purchases from a certain country

if they were paid for exclusively by imports from Russia. Such a system would be similar to German clearing and barter agreements with the Danubian countries, and it would involve at least a fear on the part of the small nations of economic dependency on Russia.

Expansion of trade with the powerful Soviet Union, marching toward economic progress and growth, might in itself signify a dynamic new era for continental Europe. It would help to re-establish the economic balance which has been so badly upset. But Europe would derive the greatest benefit if Russia entered into a world economic cooperation and supported a common policy dedicated to the expansion of world trade and to equal treatment for all trading, peace-keeping nations.

CHAPTER TWELVE

EUROPE GOES LEFT

THE SOCIAL AFTERMATH OF THE WAR

WILL THE ECONOMIC organization of postwar Europe be a system of private enterprise, state capitalism, a synthesis of the two, or a struggle between them? The question is raised in the *Economist* of January 1, 1944. It is obvious that the extensive role of government in national economy will continue for a number of years, though with various changes and different objectives. There will be foreign exchange and foreign trade control, centralized purchases of food and raw materials from abroad, control of prices and wages, a control of capital markets, systems of priorities, and so on. De-control will take place step by step according to the reconversion of production and economic reconstruction in general. Therefore, we can expect in most of the European countries a comprehensive system of direct as well as indirect controls, which will be a starting point for the planning of peacetime economy. Here, much, if not all, will depend on the eventual objectives of the respective governments, on the social climate, and on the economic system considered most appropriate by each nation for itself.

In the countries already liberated various opinions have been expressed on these matters, and there have been many reports about the programs of the resistance movements.¹ It should be remembered that these countries have been isolated from the

¹ See for instance Winifred N. Hadsel, "Post-War Programs of Europe's Underground," *Foreign Policy Reports*, Nov. 15, 1943.

rest of the world for a number of years and that they have lived under exceptional conditions without having a chance to form their opinions in the normal way. All this has certainly affected their psychology. They will have to learn the trends of opinion in the outside world in order to ascertain their own future position and role and in order to become fully aware of the complexity of the task of rebuilding and reconstruction. Perhaps without realizing it, they will have been influenced by the German political, economic, and social philosophy. Furthermore, the attitudes and the politics of their returning governments-in-exile will be of great importance. The postwar situation is bound to be in flux; every action will initiate reaction. The prestige and the influence of the United States and Great Britain on one side and of Russia on the other side will be of great significance.

After the defeat of France in June, 1940, it was feared by many that the Nazis might be able to win the support of a number of people who would be especially influenced by their economic and social program. The German principles seemed to be simple. They promised steady employment for industrial workers, steady prices and guaranteed markets for agricultural products—of especial appeal to the Danubian agriculture—and they did not hesitate to increase wages. Peace and prosperity, order and security were promised. Since then, however, the true nature of the Nazi rule has become clear, so that there is reason to hope that the consequences of the Nazi program will not be of any noticeable weight.

There is general agreement that a new and better Europe must be created, and a number of high-sounding programs have already been made public. It is certain that the nations will not want to go back to the *status quo ante*. They have been taught by bitter experience that the prewar situation—political, social,

as well as economic—was not satisfactory in many respects. The nations remember not only the unemployment and restrictive economic policy during the interwar period: the weaknesses of the whole political system, including the way of practicing parliamentary democracy in some countries, are still fresh in their memories. And the people who had suffered from German occupation will perhaps ask more persistently than the other nations: “Why was it not possible to check the Nazi aggression in time; why was Nazism not stopped at the very beginning?”

Therefore, the most important issue for the European nations will be the problem of *security* itself. They will want to find out how they can protect themselves against future aggression, how they can avoid future wars. For the small nations this will even be more important than for the big powers. At the same time, freedom for all nations, big and small alike, will be demanded, allowing for no more than just such limitations as are necessary to organize a working system of security.

In the economic field also, there is agreement on some issues. There is a wide demand for planned economy in general, but until now no detailed specification has been supplied of what such planning should include and what its objective and its machinery should be. Obviously, full employment, a rising standard of living, and comprehensive social security are generally accepted aims. The importance—yes, the necessity—of universal improvement of economic and social conditions has been emphatically underscored, while at the same time it is being stated that economic values must be subordinated to higher, such as cultural and social, values. In medieval times, the Catholic Church postulated this demand, though without promising increased wealth for all. She succeeded in putting

spiritual values before economic issues; the result was a stagnation of economic life during this whole period.

Everywhere economic reform for Europe is demanded; but most of the programs are stated in general terms and are vague as to details. In the opinion of many, Europe cannot be reformed without a revolution, specifically an economic and social revolution. The term revolution is used broadly and with diverse meanings. For some it seems to imply the achievement of an expansion of democratic rights; the abolition of class privileges and of the remainder of the feudal system; land reform and social security; government control of monopolies and big business; and new standards of housing. For many others it is almost equal to socialism. According to the latter, democratic institutions can only be reinstated in Europe if they take on a progressive and socialist character.²

It is often stated that economic democracy must be established on the Continent. But the term democracy, similarly, has no precise and generally accepted meaning. Whereas in the United States and in England a substantial amount of economic freedom, and of course of political freedom as well, is considered indispensable to a democratic system, many ardent proponents of democracy among the continental nations hold the contrary view: that extensive government control of economic life is necessary for democracy.³

It is difficult to agree on the meaning of terms; it is much more difficult to reach an agreement on the particular program to be

² See Fritz Sternberg, "The Condition of Europe," *Common Sense*, September, 1944.

³ President Dr. Edvard Beneš, expecting that there will be a definite leftward trend throughout Europe when the war is over, believes that its people will fashion a really popular type of democracy, far removed from the "pluto-democracy" derived by its critics. *The New York Times*, Magazine Section, Nov. 19, 1944.

followed. Nevertheless, it is clear that, whatever the economic and social systems of Europe may be, certain conditions will have to be fulfilled if Europe is to recover quickly and achieve greater prosperity. Production must increase for many years to come. "The size of the cake of national output is certainly as important as, and probably far more important than, any questions about the size of the various slices."⁴ Higher efficiency of production must be achieved in order to improve the level of living and to compete, for instance, with many American products.⁵ The structure of national economy must be flexible, so that it can be adjusted to changing circumstances. And, finally, the national economy should be organized in such a way as to facilitate a close economic cooperation with the rest of the world within an expanding world economy.

PRIVATE ENTERPRISE OR STATE OWNERSHIP?

Whether the national economies of the European states are organized on a socialistic or progressive-capitalistic basis with different degrees of control and planning, the main problems—or we might call the chief difficulties—and the necessity to solve them will remain without great change. Yet, often, attention is diverted from the real issues to mere forms of organization, and

⁴ *Economist*, Oct. 14, 1944, p. 503.

⁵ An example is contained in the report of the British mission to the United States to examine the cotton textile industry. The report states without hesitation that the United States industry is very far ahead of the Lancashire industry—one of the oldest British industries—in production per man hour. With normal staffing, the British output per man hour is less than the American by about 18 to 49 per cent in spinning, 80 to 85 per cent in winding, 56 to 67 per cent in weaving. The British mission investigating building methods shows that the industry is operating at lower real costs in the United States than in Great Britain. This was also found to be true of the coal mining industry. Reports of this kind illustrate how much could and should be done in European industry, if a higher level of living is to be reached.

there is danger that once more the line of least resistance will be followed. "To many people economic reconstruction appears to mean little beyond the compiling of lists of industries to be nationalized."⁶ Thus, a number of reconstruction programs lay great stress on the nationalization of industry and banks as a necessary step toward economic democracy. In almost every one of the liberated nations this question of nationalization forms an important issue, even though the situation itself differs in the industrialized countries, particularly in Western Europe, and in the agricultural countries in the East and Southeast.

Although the discussion has been going on now for several years, it has not supplied solid arguments for nationalization on chiefly economic grounds.⁷ Those usually brought forward are well known; very often they are taken from the socialist programs advocated before the first World War and in the interwar period. Some of these old arguments demand nationalization in order to achieve a better distribution of wealth—an objective which, in countries with a progressive wage and social policy and with a good fiscal policy and administration can be achieved without great difficulty. Another argument is that monopolies should not be left in private hands; but transportation, communication, and public utilities systems have long been owned by public bodies nearly everywhere in Europe. If the term monopoly is understood to include technological monopolies, does that mean that every future monopoly should be nationalized? The history of the technological monopoly shows how soon it is threatened with competition, and how short its life usually is. A very popular present argument is that the so-called key industries should not be privately owned. Here again the problem

⁶ *Economist*, Sept. 4, 1943, p. 328.

⁷ See "Why Nationalize," *Economist*, Sept. 4, 1943, p. 328.

is to determine what key industries are, and what should be done if, because of technological developments, new key industries emerge, or old ones cease to exist as such. All these current discussions are much less thorough and profound than the analysis of the economic merits of nationalization carried out in several countries after the last war.

Some new arguments are resulting from the present war. The changes in ownership of industrial property and banks carried out under the German rule are the basis of the demand on the part of some national groups for radical changes in their own economic and social systems. The assertion is made that in most cases it will be impossible to return the property to the rightful owners, and that therefore the government should assume ownership and should pay some kind of indemnity to the rightful owners.⁸ Another reason put forward for nationalization is that the Germans have destroyed the middle class and especially the managerial element,⁹ so that the government has no alternative but to take over the management of many industries. The proponents of this measure do not add, however, where the government is to recruit men capable of doing the job.

One decision has definitely been reached: The governments will confiscate property of those who cooperated with the enemy. In some such cases, very important enterprises will be affected. While the government will hardly take over a restaurant or a drugstore because the owner was a traitor, political parties may insist that it appropriate a large automobile factory or textile mills which seem to them important to the national economy. Against this it can be said that, though treason and collaboration

⁸ For more details see the author's *Industrial Property in Europe* (New York, 1944).

⁹ F. Munk, *The Legacy of Nazism* (New York, 1943), pp. 221 ff.

are undoubtedly justifiable grounds for confiscation of property, they do not present an argument for nationalization of an industry.

Radical groups throughout the Continent are blaming business for having cooperated with Fascism and Nazism even before the war. Yet, taking just one example, the vote in the French parliament after Munich was certainly significant in showing that the socialist parties backed the policy of appeasement no less than did the conservatives. Perhaps in all European countries illustrations could be found to prove the lack of determination, the weakness of the democracies, during the interwar period. Sometimes the very people who today accuse others of not fighting Germany did not themselves support the war before the outbreak of the German-Russian hostilities. Even in countries like Greece or Yugoslavia, where the government was run entirely by politicians and the influence of business was slight, business leaders are now blamed for conspiring with the Fascists. As a whole no political group should assume the right to condemn another group on the basis of a few general accusations. Guilt and responsibility should be allocated justly, as well as merit and commendation. We shall agree entirely with the punishment of all traitors and collaborators, but the attempt to condemn indiscriminately a whole class, already weakened, in order to procure an argument for nationalization of business should not be supported.

A thorough analysis would show that the decision of this important problem is not sought on economic merits, but that it has become a *political issue*. It has become once more the center of a fight for power, and is often put before genuine economic needs.

We are still waiting for a study which would clearly indicate

the economic and social merits of nationalization of industry in European countries. Such a study would be presumed to provide tangible evidence that if nationalization of industry is carried out the most important problems will be solved: full employment will be achieved more easily; efficiency of production will be improved; social peace will be obtained by agreement and cooperation; and the whole economic structure will be flexible enough to adjust itself to world economic changes. Finally, international economic collaboration will be more permanent and comprehensive than under any other economic system.

It is understandable that many socialists feel that the time is ripe for the fulfillment of their prewar program. The adjustment of the property transfers, as well as the condemnation of the business world as pro-Fascist or at least reactionary, should give impetus to their cause. But, as a political issue, the radical program will automatically provoke reaction, and it must lead to political fights. Obviously, such fights frustrate attempts at political consolidation and economic reconstruction. In the interest of an early European economic revival, it would be unfortunate if the end of the war were to be followed by the outbreak of class struggles and social upheavals. Therefore, the immediate postwar world is ill suited for such vital economic and social decisions. Some kind of truce should be accepted for the period during which the foremost task will be to revive the whole national economy and bring it back to work. European economy has not much time left to start the task of rehabilitation.

The whole issue—private enterprise or government ownership—should be approached from a new angle. The demand for nationalization of industry dates back to the general program of the Social Democrats, which is based on the dogmatic Marxian doctrine, and is still operating within the concept of the “class

struggle." In agriculture the question of ownership has been solved realistically on economic rather than political terms; at least this is basically true in Western and Central Europe. The general welfare, technological progress, maintaining employment—these are today the first objectives, and the question of private or public enterprise should be regarded as subsidiary to them. For the nationalization of industry, objective grounds should be put forward for public examination and approved. Then, if a community wants an industry to behave in a way substantially different from its behavior under private management or private ownership, the industry should be nationalized. In such a case it is presumed that, from the standpoint of the general interest, the publicly owned enterprise will be better able than the private enterprise to fulfill the set objectives. When the pros and cons have been considered, the nationalization of such an enterprise would find public support. Of course, should the sphere of nationalized industry extend too far, the problem of omnipotent government versus political freedom and democracy would promptly emerge.

If such objective approach to a problem usually regarded as political could be reached, it might be possible to take the politics out of this crucial question. By so doing, we could hope to remove the "stumbling block" that has long been so great an obstacle to smooth cooperation among all classes of economic life, and we might help to bury the old doctrinaire "class struggle." The radicals demand that the communist bogey, currently blamed for many political mistakes, should finally disappear. Equally justified is the demand for the laying of the business bogey which also is not without responsibility for a direct or indirect share in many political blunders.

The opinion is widely held that in Western and Central Eu-

rope, where industrialization went hand in hand with democratic political institutions and advancement of social welfare, reforms could be effected without fear of internal conflict. On the other hand, it is thought that in Poland, Rumania, Hungary, Greece, Bulgaria, and Yugoslavia, revolutions similar to the Bolshevik Revolution in Russia can be expected, unless far-reaching reforms are promptly put into operation.¹⁰ The peasant's firm demand for a piece of land of his own is a factor on which we have to count everywhere in the East and Southeast of Europe. It seems, furthermore, that these countries are aware of the differences in economic resources and size between them and the Soviet Union, and that this fact will prevent them from following blindly the Russian economic pattern.¹¹ It is very doubtful that replacing the German rule and a Fascist or semi-Fascist government by an authoritarian regime would satisfy the expectation of the people.

As far as we can judge now, it is probable that the number and size of industries and banks owned by the state will increase in several European countries. For various reasons, governments will find it necessary to take into custody and manage, at least temporarily, a great number of private enterprises. All this will create new problems. We sometimes hear that the management of industry in the advanced industrial countries has lost its dynamic character, that it has become merely administrative, and that it makes no great use of truly free initiative. In

¹⁰ Vera Michaelis Dean, *On the Threshold of World Order* (New York, 1944), p. 28.

¹¹ So, for instance, it has been reported that Yugoslav industries, though planned by the central government, will be organized by private initiative on the basis of private ownership. The *New York Times*, Report from Beograd, Nov. 25, 1944. See also Stoyan Gavrilovic, "The People Take Over in Yugoslavia," *Free World* Dec., 1944.

regard to the European countries such a supposition is greatly mistaken. It is true, however, that to a large extent Europe's industry will have to be reorganized, and this task will require more imagination and determination than was called for before the outbreak of the present war.

Before the war, government-owned enterprises were frequently administered like private enterprises; nevertheless, except in the field of armament and monopolies, their commercial success was not encouraging. Quite commonly—and, perhaps, inevitably—they were subject to some sort of pressure, from political parties, as well as from business groups and labor unions. Monographs dealing with the results of government-owned enterprises in various countries would be very useful right now. In countries with parliamentary democracy the attempt of political parties to get special advantages through direct economic controls introduced in the thirties is fresh in our memory. If industries owned by the government are to be as efficient as those privately owned, and as flexible as the post-war situation will require, special machinery will have to be devised to ensure that all decisions are based on economic grounds. In countries with large government holdings of industry, the economic administration must be given an independent status comparable to that of a supreme court—in other words, it must be protected against any kind of political pressure that may arise.

PLANNED ECONOMY

All experts agree that the influence of public policy in Europe on the conduct of industry, trade, and banking will be considerably extended. Planned economy (*économie dirigée*, it is now called by General de Gaulle, and was so-named by some poli-

ticians in Central Europe before the present war) has been accepted as a system appropriate to the circumstances of modern economy. Every planned economy includes various kinds of direct and indirect control, dependent upon the degree and intensity of government interference and upon the general as well as the specific objectives of planning. These objectives can be summarized as a rising level of living throughout Europe, with specific emphasis on a high level of employment in the industrial countries and speedy development in the depressed agricultural areas.

In the future, when depression threatens, the government of every country will be prepared to take action to arrest it at the earliest possible moment. The attempt will be made to maintain a steady flow of wages and income, a given level of consumption and investment expenditure to avoid unemployment and to synchronize public investment so as to offset a decline in private investment. However, it will be very difficult to control the one element in the total national budget that is most likely to fluctuate, namely the foreign balance. "A country dependent on exports needs prosperity in its overseas markets. This cannot be achieved without effective collaboration among the nations," says the British White Paper on Employment.¹²

Employment in all highly industrialized countries from which important parts of production are usually exported is subject to the fluctuations of international trade. Such countries are expected to resort to various measures to stabilize employment. Yet the respective domestic policy may bring about distortions in prices and production that may prove to be new obstacles to foreign trade.¹³ The policy of high-level employment in small

¹² *Employment Policy* (New York, 1944), p. 4.

¹³ The British White Paper says rightly (p. 18): "If important British exports

countries depending on export cannot rely on devices effective in such large economic units as the United States. A coordinated antidepression policy of the leading industrial powers would be of enormous help in guiding the policy of the smaller nations.

Many countries will attempt to increase their exports mostly by virtue of necessity, but they will at the same time make great efforts to expand their domestic markets. This could certainly be done best if coordinated with the expansion of foreign trade. At any rate, there are great possibilities of developing markets in most of the European countries. If we compare each particular country with Great Britain or the United States as to consumption per head of many articles of daily use and a great number of durable consumer goods, we shall see that the margin for increasing the markets in these countries is great indeed, and that much of it could be done by domestic production. It requires, of course, a policy systematically aimed at expanding markets; in some countries this would necessitate a basic change in the patterns of thought of the people. Granted a freer trade policy, it remains to ascertain what conditions must be fulfilled in order to achieve higher production and consumption. The first steps would be higher real wages—their interdependence with a higher output is evident; it must be determined what measures are necessary to improve the efficiency of production. Throughout the whole national economy, the old policy of restriction would have to be substituted by a policy of expansion. The Continent of Europe did not have vested interests only in big business, as is usually stated: vested interests existed also in agriculture, in commerce, even in handicrafts and bureauc-

fell off sharply, it would be essential, at the earliest moment, to find alternative exports to fill the gap: an expansion of internal demand would not alone be an appropriate remedy and, indeed, if it were applied too vigorously, might lead to inflation."

racy. In a number of European countries there were still remnants of feudal habits; the economic philosophy of small town politics and civil servants, dwelling mentally in the old good days, was present alongside the paraphernalia of modern large-scale industry. Only when the economic life is liberated from the obstacles and shackles that, often unseen, have hampered modernization and commercialization, can expanded markets be achieved.

Similarly, the fiscal policy will have to be subordinated to the new dynamic economic policy. In many European countries, and especially in the poorer ones, the tax system has been a regressive one; high taxes and custom duties on daily consumer goods as sugar and coffee, a general sales tax, and taxes on coal and transportation are a few examples of a system that was ill coordinated with the real needs of the national economy.

It would be of the utmost advantage if labor unions would join the government and business in a thorough examination of the ways and means of achieving a higher standard of living. In the past, the socialist parties concentrated only too often on gaining political power and securing social legislation, instead of striving first to raise the standard of living. Experience has clearly demonstrated that the best social legislation, including social insurance, is not enough when real wages are low or there is prolonged unemployment. In the present era, when governments are willing to assume responsibility for providing employment, there is perhaps a better chance to bring together representatives of labor unions and socialist parties with representatives of government and business for the purpose of examining these chief problems of employment and living standards.

It is difficult to foresee how far the governments in the individual countries will go in using direct or indirect control of

the national economy. In the concluding paragraph of the White Paper on Employment¹⁴ the British government says that it believes that, once the war has been won, we can make a fresh approach, with better chances of success than before, to the task of maintaining a high and stable level of employment without sacrificing the essential liberties of a free society. The pattern of planned economy will in all probability differ from country to country; the economic and social systems in postwar Europe may be more manifold than before the war. The number and size of industries and banks owned by the state will increase perhaps more in Eastern than in Western Europe. While in some countries planned economy in peacetime will resort prevailingly to indirect controls—following the example of the New Deal or the expected British policy—in other countries direct controls may be developed rather extensively. At present it is generally assumed that Eastern and Southeastern Europe will belong to the second category. As one observer has recently stated, industries will be largely state owned and state controlled, and capitalism as known in America will not exist there. For the small businessman there will probably be as much scope as for the worker and the peasant.¹⁵

In view of the expected variations in economic organization in the European states, it is important that no new obstacles to mutual trade relations should be introduced and that barriers to the adjustment of production should be avoided. The extension of state ownership of industry, an uncoordinated policy

¹⁴ *Employment Policy*, p. 28.

¹⁵ Edgar Snow, "Eastern Europe Swings Left," *Saturday Evening Post*, Nov. 11, 1944. In his article, "Czechoslovakia Plans for Peace," *Foreign Affairs*, Oct., 1944, Dr. Beneš expresses his expectation that the principles of individual property, private enterprise, and freedom of trade will not be violated, even though a certain degree of economic intervention and *étatization* (for instance in armament industries) proves desirable.

towards expansion of domestic markets, and the direct control of business might easily perpetuate a restrictive foreign trade policy. The experience of the decade before the war does not warrant a strong assumption of foreign trade expansion if there is substantial government intervention in regular business transactions.

The nations in Europe will have to realize that so-called domestic problems have ceased to be purely domestic.¹⁶ In their own interest they will have to coordinate their national policies; the objective of expanded production demands such coordination. Common, concrete schemes for European production and trade are vital for the future of the Continent and for peace. Only if the national policies of the European countries are conducted in this spirit, will fruitful cooperation develop between even very different systems; such cooperation will bring them nearer to each other.

¹⁶ Arnold Wolfers in "The Outlook for Europe" (*Yale Review*, Winter, 1944, p. 208), expressed the opinion that, whatever the outcome of the social struggle now in progress in many parts of Europe, the Old World will for many years face one of the gravest crises in its history.

CHAPTER THIRTEEN

A NEW EUROPE AND WORLD MARKETS

WE CAN NOW briefly summarize our findings with regard to the expected economic situation of the European Continent after the war. The amount of physical destruction and exhaustion will be incomparably greater than after the first World War; and greater indeed will be the need for relief and rehabilitation and the task of reconstruction. Europe will be faced with great economic changes. The industrial developments of many countries will at first reduce export possibilities of a number of goods from Europe, though increasing demand for other commodities, and, even in third markets, competition from newly erected or expanded industries will appear. Since Great Britain had occupied an extremely important role in Europe's foreign trade, the changes in her economic and financial situation will bear upon the European economy. Germany will have lost her dominant position. For several years to come, she will not be the former efficient competitor on the world market; at the same time she will also cease to be a substantial buyer of many commodities exported by other European nations. As favorable factors in international relations, the increase of trade with the Soviet Union should be mentioned first. It would help greatly in offsetting Europe's difficulties, as would also an intensification of commercial relations with the Near East. Furthermore, countries now possessing sterling balances will provide sustained markets for British goods. Greater demand for foreign commodities will also come

from countries which, during the war, have increased their gold and dollar balances—though a great part of these funds may be spent on American goods before European countries are in a position to export their products on a large scale.

The economy of Europe will have to adjust its structure to all these new conditions. Moreover, this will have to be done after the most costly war—in lives, in goods—has wrought startling changes in the economic and social systems of many nations. It is unfortunate that these events, which by many are called revolutionary, fall at a time when Europe as a whole is forced to reorient her economy and to make a determined effort to regain her previous place.

It is evident that the readjustment of European production and trade and the achievement of an economic world equilibrium will require time, and will only be possible if world production and world trade expand simultaneously. This is vital to Europe's economy; only within the framework of an expanding world trade will there be room enough for European products. Fortunately, the demand for such expansion is heard not only in Europe but all over the world, and is recognized as in the interest of all. Great Britain's position is obviously similar to that of the industrial countries of the Continent. The United States is definitely in favor of expanding world trade, because it is indispensable for her greatly enlarged industrial production.¹ So, also, are the primary producing countries, whose higher production likewise needs larger markets. Thus it is natural that the main countries of the world, including Russia, have arrived at the conclusion that expanded world trade and economy are

¹ The report of the National Planning Association, *America's New Opportunities in World Trade* (Washington, D.C., 1944) p. 49, gives some examples of the magnitude of wartime industrial expansion in the United States.

absolutely necessary for establishing a new economic world equilibrium, for providing employment, and for maintaining peace.

THE REORIENTATION OF EUROPEAN PRODUCTION

Therefore, expanded world trade is regarded as the basis upon which the adjustment of European production can be realized. The eventual objective is clear and the task looks plain in itself. If a country has lost the foreign market for a definite commodity because the demand is being met by new domestic production, it must reallocate its resources, in labor as well as in capital, to the production of new commodities which can find markets abroad. Doubtless, there will always exist a potential demand great enough to absorb new production. Europe will have to maintain and intensify her development—already strong in the interwar period—towards a further specialization of production and particularly of export. The industrial structure of a number of countries will have to be reorganized in order to make a new international division of labor possible. They will be compelled to concentrate on the production not of staple goods but of specialties, which require a high degree of skill and tradition, and which are accorded a high value for the labor expended on the finished article. There is little doubt that the industrialized European nations possess the qualities needed to perform this reorientation. Their labor is skilled, devoted to its task, and usually modest in its demands; and the business world has learned to work under difficult conditions during the last decades. The small countries, having the disadvantage of a small home market, are usually more flexible and adjust more readily than the large countries.

It would be wrong, however, to gloss over the fact that the

difficulties of large-scale changes in the structure of production are considerable. This can be proved by many examples, as, for instance, that of the British industry. After the last war the export of cotton goods was greatly hit, and the export of coal and iron was becoming more difficult. Great Britain shifted to new industries—automobiles, chemicals, and electrotechnical appliances, instruments, and machinery. Between 1910 and 1938 the share of textiles and apparel in the total export of Great Britain fell from about 38 per cent to less than 25 per cent; exports of machinery, electrical appliances, vehicles, and chemicals rose from less than 14 per cent to nearly 40 per cent. Nevertheless, the volume of trade attained in 1913 was never regained after the war; it reached 90 per cent in 1929 and only 75 per cent in 1937.

Another example is Czechoslovakia. With a population of about 15 million, Czechoslovakia, before 1918 supplied the whole Austro-Hungarian Empire, whose population was 52 million. A large part of the previously protected home market had become a foreign market where Czechoslovak industry had to compete with foreign industries under equal conditions and, very soon, with sometimes highly protected new domestic production. The foreign credit influx in Central and Southeastern Europe in the twenties concealed this new situation by greatly inflating the purchasing power of most of these states. In the thirties, however, Czechoslovak industry was faced with the problem of reorienting production and export to more distant markets. Although she succeeded in increasing the share of her export to Great Britain, the United States, and most of the overseas countries, she was not able to regain the volume of her export before 1913 and 1929; her share in world exports declined from 1.84

per cent in 1929 to 1.60 per cent in 1937. The difficulties which confronted the readjustment of the Austrian economy after 1919 are well known.

Even if the nations pursue a determined policy towards transforming the structure of production and of export in particular, the transformation will require many sacrifices and a certain lapse of time. It would necessitate a detailed analysis of the economic structure of the European countries, of the situation of the various parts of production, and of the impact of the economic development during the war on these factors. The position of the European countries with regard to the problem will not be the same.

Very different problems confront France and Italy, for example. A substantial share of France's export was specialized, and many of her products will easily regain their old markets. As her economy is well balanced and her resources are more ample than those of Italy, she will be less dependent than the latter on export. Moreover, she has been a creditor country over a long period. More than a quarter of the French exports (28 per cent) went to French overseas territories, and this trade can be substantially expanded. On the other hand, because of her economic structure and a population exceeding that of France, Italy's standard of living and employment is more dependent on export. Her trade before the war was only just over half the value of French trade in 1938 and, for a number of years, was less than the trade of Belgium and the Netherlands. The policy of increased protection, aiming at self-sufficiency in food, was undoubtedly responsible for this. Although a debtor nation, Italy always had an import surplus. The export pattern was rather weak; about one third comprised raw and processed foodstuffs,

and one third, textiles. The whole export was highly competitive, with semi-luxury goods occupying a large share of it. An extensive reorientation of production and export will be necessary, and it will require import of capital and technical assistance. In many respects Italy will have to start from scratch, and the process itself will call for a certain period of transition. The destruction of her productive machinery by war has aggravated the already difficult situation.

The speed and the degree of adjustment of production in every single country will depend on several circumstances. In countries like Switzerland where before the war the exports were already diversified and specialties held a substantial share in the total export, the adjustment will be easier. Czechoslovakia may also be cited as an example of a country with highly skilled labor and diversified production, exporting at the same time high quality goods, including many capital goods, and cheap mass products like textiles, shoes, glass, and chinaware. In addition, she produces some specialties which are bound to find again their previous markets.

Thus, in country after country, we could point to strong and weak items in the export structure, items that will probably be continued or even multiplied, and others the export of which is threatened by developments in other countries. There is no doubt that, given the needed time and led in the right direction, industrial production in the European countries can be reoriented and shifted to commodities with a good prospect for export. As we have seen, Europe was exporting a wide variety of goods before the war. Those of largest value were machinery of all kinds, textiles, chemicals and pharmaceuticals, and iron manufactures, followed by instruments and watches, paper,

glass, glassware, earthenware, and china.² The export of textile goods, the production of which is increasing throughout the world, represented an important part of the export of Italy, Czechoslovakia, France, Belgium, Switzerland, and Austria; machinery, products of iron and steel and metallurgical industry had a substantial share in the export of Germany, Sweden, Austria, Belgium, Czechoslovakia, and Switzerland. In many of these fields a reorientation will be necessary.

All countries will do well to consider carefully the future possibilities before rebuilding industries destroyed by the war. A coordinated program for all the European countries is indicated; further specialization of production and export is needed. Europe's strength will lie in highly specialized goods with great labor value, to be sold to the industrialized countries. Her cheap mass products might for a certain time find markets in the newly industrialized areas. The greater the diversification of European export and the greater the proportion of capital goods and luxury or semi-luxury specialties (instead of mass consumer products) the greater the risk of cyclical fluctuations. In consequence, greater efforts will be made to expand the domestic market. Stable employment in the important industrial markets

² According to the figures given by Cleona Lewis, *Nazi Europe and World Trade* (Washington, D.C., 1941), p. 193, the export from Germany, Austria, Belgium-Luxembourg, Czechoslovakia, France, Italy, and Switzerland in 1937 was (in million dollars):

Textile goods, yarns, apparel	733.7
Machinery of all kinds	586.3
Vehicles including ships, automobiles	257.9
Iron tools, iron manufactures	300.
Chemical and pharmaceutical industry	578.4
Instruments and watches	142.3
Paper	109.
Glass and china	130.9

abroad and the mitigation of price fluctuations of raw materials and foodstuffs will be of vital interest to all European exporting nations. Their export, increasingly sensitive to all changes abroad, will force them to take part in any international cooperation that tends to make markets more stable.

CHAPTER FOURTEEN

THE ROLE OF THE UNITED STATES IN WORLD ECONOMY

THE EXPANSION of world production and world trade is now generally recognized as the way to establish, in the long run, a new equilibrium in world economy. Everyone agrees also that the resources throughout the world are ample to warrant expanded production; all that is needed is an appropriate organization and mechanism. Furthermore, it is commonly agreed that expanding world production would achieve the best results if the principle of comparative advantage is followed. And nobody has proved as yet that it cannot be done.

To achieve it on a universal scale, an appropriate commercial policy of expansion, replacing the prewar policy of restriction, is the primary prerequisite. We cannot expect that the European countries will lead the way in starting a freer trade policy. They will not have the economic strength to do so, and they will need a mighty impetus from without. It is obvious that the initiative must come from the leading economic powers, primarily from the United States.

The events of the thirties have clearly shown that commercial policy is tied up with the problem of unemployment. It has been proved that a restrictive foreign trade policy cannot cure unemployment but, on the contrary, has a tendency to aggravate it. Moreover, it has become evident that it is extremely difficult to move towards freer trade as long as substantial unemployment exists. It is a vicious circle: in many countries employment will not rise unless international trade increases; but the fear of

unemployment itself hampers, if it does not prevent, the introduction of the liberal policy needed to increase world trade. It is imperative, therefore, that steps towards liberating trade be taken during a period of high employment; the maintenance or extension of employment will then be automatically aided. An increase of world trade is expected from the development of the retarded regions, which will need to import capital for that purpose. Thus the policy of freer trade, of high level employment, and of development of backward areas can all be co-ordinated and should work to the same end.

It will depend in the first place on the United States, as the most important economic and financial power in the world, whether such an economic program, accepted by the United Nations, can emerge immediately after the war. This responsibility will be manifold. The experience of the thirties has shown us the importance of American business activity for the entire world trade. It has been stated correctly that the decline in national income hit American imports harder than did the high tariffs. The maintenance of a high national income is, therefore, a primary condition for a high level of imports into the United States. In the first years after the war, the world will need many more goods from the United States than it will be able to sell to her or to pay for. The granting of credits and direct investments abroad will help to maintain employment, particularly in the capital-goods industries enlarged during the war. This export of goods, financed partially by credits and investments abroad, will help to rebuild countries damaged by the war, and will accelerate the economic development of the retarded regions.

The development of American foreign trade and investment policy will have great importance for the Continent of Europe

in several respects. Of foremost consideration is the expected financial assistance in the rehabilitation and reconstruction of Europe; secondly, there should be good possibilities to increase exports from Europe to the United States; an enlarged American import of raw materials and foodstuffs from other parts of the world would increase the prospects of European export to those same countries; finally, the economic development of the retarded regions—aided by international financial assistance coming mostly from the United States—would create export possibilities for European products.

Even during the low level of American trade in the thirties the United States was an important market for Europe. In 1938 she bought 13 per cent of continental Europe's export with the rest of the world (11.8 per cent in 1928), as compared with nearly 35 per cent bought by Great Britain and 17 per cent by Latin America. During the period 1935–1937 all the industrial countries of Europe sold to the United States 5 to 10 per cent of their total export, with the exception of Germany and Austria.¹ On the other hand, Europe was still the most important market for the United States, taking, in 1938, 25 per cent of her total export (30 per cent in 1928). Great Britain took 17 per cent—that is, Great Britain and continental Europe together took 42 per cent of the total American export, each having a large import surplus in this trade. The Latin American countries together bought 18 per cent of the United States export in 1938 (17 per cent in 1928), or only a little more than the greatest

¹ Of total national exports, the proportion sent to the United States from several countries was: Greece, 16 per cent; Sweden, 11.8 per cent; and Norway, 10.2 per cent. Then follow (in per cent of the total): Finland, 8.9; Czechoslovakia, 8.7; Italy, 8.5; Switzerland, 7.5; Belgium, 7.2; Spain and Portugal, 7. Germany sold only 3.7 per cent of her total export to the United States, and Austria 2.3 per cent.

single customer, Great Britain. The 23 per cent supplied by the European Continent compared well with the 26 per cent supplied by Latin America. These figures illustrate sufficiently the importance of the mutual trade relations between Europe and the United States.

The prewar level of the American foreign trade is now generally considered as too low. It is realized that a much greater export will be needed to ensure satisfactory employment. It has also become evident that foreign trade is a two-way traffic and that enlarged export will only be possible if the foreign countries have the means to pay for it. Most countries have heretofore concentrated their attention on the promotion of exports; but, for the United States, a nation whose balance of payment has a different structure from that of, for instance, Great Britain, it would be no less important to find ways to promote imports, because by doing this she will automatically assist her exports.

Predictions have been made concerning the expected level of foreign trade of the United States after the war. One such prediction was made by the Department of Commerce.² Under the assumption that domestic economy will function at capacity level, it is calculated on the basis of past relationships that imports in the hypothetical postwar year 1948 would total about \$6.3 billion in terms of 1942 import prices. Other payments to foreigners—for services and through the investment of American capital abroad—might be expected to amount to some \$4 billion under the same condition, so that the total amount made available to foreign countries would be \$10.3 billion. American export is calculated to reach \$7 billion—nearly double that of the thirties.

A recently published report of the National Planning Associa-

² *Foreign Trade after the War* (Washington, D.C., 1943).

tion ³ sets the figures for 1950 at exports of \$7 billion and imports of \$5 billion, in 1941 prices, under the assumption that the American general prewar policies in regard to tariffs, export-promotion credit and other foreign trade issues are to be continued after the war. The report states that "the continuation of the present commercial and financial policies will not facilitate foreign trade in a volume sufficient to make the important contribution that foreign trade can and should make to the maintenance of domestic full employment." The legitimate demand for American goods and capital for reconstruction and development alone may approximate \$7-8 billion yearly. The United States will possess the capacity to meet this great demand: its use is needed if full employment is to be maintained. Therefore a "foreign trade budget" for 1950 is proposed, providing for exports of \$10 billion and imports of \$6 billion. A balance of \$3.7 billion will be filled by net capital outflow for a period of ten to twenty years, \$3 billion of which would be represented by long-term capital. The report says that "a failure of the United States to export capital at a rate substantially greater than \$1 billion a year would be little short of disastrous from the world viewpoint."

In this and similar calculations of the level of the American postwar export, the export of capital from the United States plays a most important role. There is no question about the need of this capital throughout the world. The National Planning Association ⁴ considers entirely possible an \$18 billion export of capital from the United States to Europe in the first ten years following the war. There can be no doubt that export of capital

³ *America's New Opportunities in World Trade* (Washington, D.C., 1944), p. 28, 48 ff.

⁴ *Ibid.*, p. 53.

would raise American exports to record levels as it did in the twenties—and that it would provide not only employment but also a grace period during which the distorted industrial structure in the United States could be corrected in an orderly manner. American credits and investments are indispensable indeed for world economic reconstruction and development. They will provide a grace period also for the European economy, during which the readjustment to the new conditions in the world markets in addition to the task of rebuilding can be carried out.

Yet it should be clear that a creditor nation cannot support its export surplus indefinitely with the export of capital. Eventually an adjustment of the balance of payments must be made to fit the pattern of a creditor nation. Invisible items of the balance of payments will not be sufficient; imports will remain the key to the problem of balance of payments. Without greatly increased imports, no durable basis for an extended export from the United States can be established. It is clear that American economy must also be adjusted to the new position of the United States. It will not be enough to import raw materials and foreign products that do not compete with domestic production. American production, too, must follow the principle of comparative advantage, and curtail industries whose products can be manufactured more efficiently abroad.

If the national income reaches the expected high level, and a satisfactory employment is obtained, it should not be too difficult to make a substantial increase of imports possible. Proper measures have to be taken in this respect; long-range planning must be undertaken, and the traditional attitude of the American people toward import must undergo a profound change.

Fortunately, the United States is economically and financially strong enough to help the world economy throughout the diffi-

cult postwar period—with all its political and social complications—and to provide for a breathing space until a new world economic equilibrium is established. This will be possible only if the national economies of all important nations, including that of the United States, are readjusted to the new conditions. Such equilibrium, based on an enlarged volume of world trade, will provide enough room for the needed increased export of continental Europe, Great Britain, and the United States. If the threat of a new crisis to the whole structure of world economy is to be avoided, prompt concerted action must be taken.

CHAPTER FIFTEEN

A MULTILATERAL APPROACH

THE UNITED NATIONS are endeavoring to establish a political as well as an economic organization to promote international cooperation and maintain peace. Assuming that the general political organization proposed at Dumbarton Oaks will be created, and that the monetary and financial proposals of the Bretton Woods Conference will be carried out, there remains the need for a comprehensive arrangement to settle the problems in the vast field of international trade. To leave all matters to bilateral negotiations between the states concerned might result in long delays and possibly, even, in a false start.

A good basis for the preparation of multilateral agreements is offered in the principles of Article VII of the Mutual Aid Agreements. In the agreement concluded between the United States and the countries receiving Lend-Lease supplies, action to be agreed upon by the countries is envisaged as "directed to the expansion, by appropriate international and domestic measures, of production, employment, and the exchange and consumption of goods which are the material foundations of liberty and welfare of all peoples; to the elimination of all forms of discriminatory treatment in international commerce and to the reduction of tariffs and other trade barriers."

The basic economic philosophy expressed in these terms should be taken as the starting point for negotiating a multilateral convention for liberalizing world trade. Reduction of all kinds of trade barriers and a firm establishment of the principle of trading equality should be the guiding concepts. It is obvious

that concord on these principles between the United States and the United Kingdom is an indispensable condition of the whole program.

In Great Britain, members of the government, businessmen, labor leaders, and economists all emphasize the need of a wide increase in British trade, and they realize that such an increase can only be brought about within a general trade expansion. Yet the uncertain position of the British balance of payments, coupled with the fear of American competition, is responsible for the doubt—expressed publicly by economists, leading periodicals, and industrial organizations—whether Great Britain will be able to return to a universally multilateral trade and whether she will be able to maintain fully the most-favored-nation clause and to eliminate quantitative trade and exchange restrictions.

It has been suggested that Great Britain should make use of her bargaining power as a large importer and also of her present position as a great debtor within the sterling area to induce her creditors and those from whom she buys to take more goods from her. Agreements similar to bilateral clearing arrangements, only on a larger territorial basis, were mentioned. It has been repeatedly asserted that such agreements could operate towards an expansion of trade between the members of the sterling area without damaging trade relations with other countries.

The sterling bloc¹ which was established during the war to help Great Britain to finance her imports and other payments abroad, provides, in addition to settling mutual sterling balances, for a pooling of dollars and other free exchange (hard

¹ The sterling bloc included at the end of 1944 the whole British Empire except Canada and Newfoundland, British Protectorates and Mandated Territories, Egypt, the Anglo-Egyptian Sudan, Iraq and Iceland.

currencies) resources. These income items are converted in sterling, and nearly all members of the bloc possess claims (sterling balances) against Great Britain. While the sterling balances can be used without significant limitations within the sterling area, a special permit is necessary for allocation of foreign exchange needed for import of goods from non-sterling-area countries. The discrimination in favor of the sterling-area trade is clear; a result of war emergencies, it was not much felt or resented under the exceptional trade conditions in wartime.

It is doubtful whether members of the sterling bloc will be willing to continue the existing set-up, especially if it meets with the disapproval of the United States. Some of these countries, notably India, are already demanding free disposal of their income in dollars and a partial conversion of the sterling balances in dollars. Special arrangements will be necessary. To continue the organization and policy of the sterling bloc after the war would be considered by other powers as trade discrimination. It should be clear, however, that Great Britain will have to succeed in consolidating her large sterling debts before she can decide on her future foreign trade policy and abandon the present possibilities, considered by some as making an increase of trade more certain than a general multilateral system, especially if other countries join the sterling bloc. It has also been frequently pointed out that Great Britain cannot commit herself to any definite commercial policy as long as uncertainty exists about the future commercial policy of the United States, and as long as large fluctuations in American economic activity remain as a menace to world trade.

As these opinions in Great Britain grow stronger,² and as, at

² See "The Principles of Trade," *Economist* (Jan., Feb., 1944); *International Trade Policy*, Report of the Federation of British Industries, 1944; *World Trade*,

the same time, the necessity of collaboration to achieve an increase in world trade is recognized, it becomes more and more urgent to reach an agreement between the two countries and for the United Nations to negotiate a multilateral trade convention. Such a convention should aim at the effective and substantial reduction of all sorts of barriers to trade. It should eliminate all forms of discriminatory treatment in international commerce, reduce import tariffs, and achieve the progressive elimination of quotas and prohibitions against exports and imports. Furthermore, it should lay down freer rules of trade with reference to government monopolies and state trading, including trade between countries where private enterprise prevails and those where foreign trade is managed by the state. In international trade organization should be created to study international trade problems and to recommend practical solutions.³ It is to be hoped that Russia will find it possible to join such a system of international trade. She, too, must be interested in a great revival of international trade and, in the long run, she will also benefit from the application of the principle of equality of trading opportunity.

There are, of course, many who harbor serious doubt whether such a broad program is at all feasible. First, they point out that we cannot presume that the European nations will feel safe enough to commit themselves to a policy of freer trade and to renounce the many weapons of restrictive trade practices; they will at least not do so before they are able to appraise the trend of world trade. Without doubt, a special regime will be needed

Report of the British National Committee of the International Chamber of Commerce (1944); Richard Schüller, "Great Britain's Trade Policy," *Social Research* Sept. 1944; *Economist*, Jan. 13, 20, 1945.

³ See the Committee on International Economic Policy's *World Trade and Employment* (New York, 1944).

for the period of transition. The Final Act of the "International Monetary Fund," agreed upon at the Bretton Woods Conference in 1944, proposed that, for a period of five years after the start of the Fund's operation, exchange control on other than capital transactions be permitted. Similar provisions for the period of transition relating to foreign trade can be included in the envisaged Trade Convention which would reduce the barriers step by step. The main point is that the United Nations should have a definite program and that they should carry it out consistently.

Another objection underlines the difficulties arising from government monopolies and state trading versus systems where private enterprise prevails. It is certain that provisions aiming at more liberal trade could be simpler and more direct under a uniform system such as existed before the first World War. Our task, however, will be to work out some correlation between the different systems that would make fulfillment of the main objective possible. And here all will depend on the basic intention of the parties; if they are determined to go the way of trade expansion, then the machinery to achieve the goal can be established. Only by practical cooperation can the nation become better acquainted with the different economic and trading systems in force; the differences can then be narrowed down by experience, and the platform for cooperation can be enlarged.

There are those who think that State monopoly in foreign trade started with the final breakdown of the traditional balance of power system on the European Continent in 1930-1931, and that a new political set-up in Europe will make the reintroduction of freer multilateral trade very difficult.

The concepts underlying such opinions have basic similarities

to proposals to divide the Continent of Europe, at first politically and later economically, into two spheres of influence, one British and one Russian. The thesis continues: The strategic lesson of this war has created the desire for closer and more permanent union between Great Britain, France, Belgium, and Holland—to which Norway and Denmark are currently being added. The countries neighboring on Russia should presumably look to her for protection, and her sphere of influence is supposed to extend to Finland, Poland, Czechoslovakia, Hungary, Austria, Yugoslavia, Rumania, and Bulgaria. While close cooperation in political affairs among the countries of the British sphere is regarded as easily realizable, the problem of close association in economic matters seem to present greater difficulties.⁴ This applies especially to the mutual trade of these countries. Although a unified market of more than 120 million people—not counting the colonial dependencies—should be considered beneficial to the participants as well as to the world at large, the British themselves doubt whether it will be possible to establish a customs union with all these nations. And there is little doubt that a preferential system would provoke strong opposition everywhere. On the other hand, there may be some who would favor the creation of such blocs as facilitating economic integration and readjustment. They may point out that the Western countries of Europe, together with Great Britain and some parts of the Commonwealth, could form a very powerful economic unit with vast markets and supplies of the most needed products. At the same time, Russia could easily provide a market

⁴ "More Perfect Union," *Economist*, Oct. 7, 1944, p. 466. Walter Layton, *How to Deal with Germany*, p. 64; Arnold Wolfers (in "The Outlook for Europe," *Yale Review*, Winter, 1944, p. 206), points to the serious danger if the exponents of exclusive influence zones should some day gain the upper hand.

for the countries of Eastern and Southeastern Europe and, by adjusting their economies to her own, could organize another big economic power.

Surely many will suspect that the establishment of these two spheres of interest so frequently mentioned would divide Europe into two big blocs—a wealthy group of countries under the British hegemony and at present a largely undeveloped group in the Russian orbit. Instead of working toward a better economic integration of Europe, this would lead to a sharper cleavage than ever, particularly if it were accompanied by ideological differences and dissimilarities in the economic systems.

It would seem that all who propose or visualize such blocs overlook one important item, that the politically mature European nations will never acquiesce in such a division. Offering no hope of a solid structure of peace, it will have no interest for them. It might easily lead to competition, jealousies, and conflicts between the two big blocs. Political alliances might be concluded, but without basically changing the economic structure and trade of the partners. For instance, history has shown that before 1914 Russia, while having an alliance with France, entertained large trade relations with the Central Powers (Germany and Austria-Hungary). Political agreements which, let us hope, will all be made a part of a general security agreement, should not be of such nature that they would form an obstacle to the needed reorientation and integration of the European economy.

This hope was strengthened by the Crimea Conference at Yalta in 1945, which put a new emphasis on the importance of a general organization and on the joint responsibility of the Big Powers with regard to the economic reconstruction of Europe.

THE TASK AHEAD

The road Europe has to travel is a long and difficult one. She is more dependent on international trade than Russia or the United States because her import demands for foodstuffs and raw materials can only be met by exports of goods and services—that is, products of Europe's labor. Ultimately, domestic employment remains dependent on international trade to a degree that cannot be discounted. After two world wars the Continent of Europe has lost much of its prominent position in the world economy, but in view of its role on the world political as well as economic scene, it has still a very important place in it.

Europe will have to readjust its economic structure, in the first place its industrial structure, to the changed conditions of the world economy in order to make possible a new international division of labor, a new economic equilibrium. This process of reorientation in itself requires often painful operations. The European nations will need foreign assistance for rehabilitation and reconstruction; it is up to them to create conditions favorable to acceleration of the process of readjustment. Neither ultranationalism nor social radicalism is very helpful in undertaking a task of such magnitude. The European nations will proceed in the right direction if they are confident that world economy will be so organized as to enable them to obtain the place in international trade which they need. Only an expanding world economy and trade will bring new customers for Europe's production, for its labor. On the other hand, a contracting international trade would press Europe into a policy of self-sufficiency, accompanied by a reduced standard of living and political as well as social instability. The expansion of world trade must be planned without delay, as it is vitally important

to prepare for it during the general demand for goods which can be expected right after the war. It is desirable to orient the trade policy of the leading powers in this direction, and thus to influence the reconstruction work of the European nations in the right way.

A coordinated international trade and financial policy will be one of the powerful instruments of the international political and economic machinery; its measures must all be rooted in the same purpose—to attain increased political security by permanent mutual cooperation and to improve the living standards of the nations. All parts of the total organization are interdependent, interlocked; one cannot work successfully if the others are not cooperating harmoniously. It is clear that expanding world trade will depend on the reestablishment of a multilateral system in which the United States is ready to accept an increasing volume of imports and maintains for a number of years a steady flow of long-term capital. If, on the other hand, the United States is not in a position to pursue an economic policy consistent with its role in the world and to take over leadership in world cooperation in this regard, the disintegration of world economy will continue. The formation of big political and economic blocs will be, perhaps, the next step, as economic warfare takes on new forms and general political insecurity prevails all over the world. It goes without saying that the Continent of Europe would suffer more than other parts of the globe from such a development.

Notwithstanding the international plans for permanent economic cooperation, it is equally necessary to work on an immediate program for continental Europe. For that we must look at the European economic problems in their entirety and work out a suitable program. Such a program should realize the

necessity and the great opportunity of integrating Europe economically within herself and with the rest of the world, and it should present concrete and, so far as possible, common schemes for European production, employment, and trade.⁵ Unless this work is started very soon, it may again be too late. Of course, economics cannot be separated from politics, and the political situation will influence decisively the economic outlook.

If all these issues could, like an engineering project, be turned over to expert technicians, a system for a satisfactory solution could certainly be produced. It can easily be proved that the purely technical and economic factors could be manipulated to create a world trade expansion greater than that of the nineteenth century. However, the main problems will not be decided by experts and technicians, but by political forces. Great political wisdom will be needed to enable mankind to harvest what technology and culture are ready to provide for it within a system of freedom. Otherwise strong, and often irrational forces may once again swerve us from the road to productive work, decent living, and peace. The Continent of Europe, having gone through two wars and suffered and lost more than any other part of the world, is hardly strong enough to sustain the effects of further vital changes that do not provide first for the means of livelihood and the security as well as the freedom of the European peoples.

⁵ "It is my earnest hope, though I can hardly expect to see it fulfilled in my lifetime, that we shall achieve the largest common measure of integrated life of Europe that is possible without destroying the individual characteristics and traditions of its many ancient and historic races." From Prime Minister Churchill's broadcast on March 21, 1943.

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